1977

Illustrations of accounting for marketable equity securities : a survey of the application of FASB statement no. 12; Financial report survey, 12

Hortense Goodman

Leonard Lorensen

FINANCIAL REPORT SURVEY 12

J. T. Ball
Stamford CT

Illustrations of Accounting for Marketable Equity Securities

A survey of the application of FASB Statement No. 12

By Hortense Goodman, CPA
and
Leonard Lorensen, CPA

AICPA
American Institute of Certified Public Accountants

AICPA
American Institute of Certified Public Accountants

FINANCIAL REPORT SURVEYS

1 **Illustrations of Accounting Policy Disclosure (1972)**
A survey of applications of APB Opinion No. 22

2 **Illustrations of Reporting Accounting Changes (1974)**
A survey of reporting under APB Opinion No. 20

3 **Illustrations of Reporting the Results of Operations (1974)**
A survey of applications of APB Opinion No. 30

4 **Illustrations of Interperiod Tax Allocation (1974)**
A survey of applications of APB Opinion Nos. 11, 23, 24, 25 and SEC Release No. 149

5 **Illustrations of the Statement of Changes in Financial Position (1974)**
a survey of Reporting Under APB Opinion No. 19

6 **Illustrations of the Summary of Operations and Related Management Discussion and Analysis (1975)**
A survey of the application of Rules 14a-3 and 14c-3 of the Securities Exchange Act of 1934 in annual reports to shareholders

7 **Illustrations of Departures from the Auditor's Standard Report (1975)**
A survey of the application of Statement on Auditing Standards No. 2

8 **Illustrations of the Disclosure of Related Party Transactions (1975)**

9 **Illustrations of the Disclosure of Subsequent Events (1976)**
A survey of the application of Section 560 of Statement on Auditing Standards No. 1

10 **Illustrations of Accounting for Contingencies (1976)**
A survey of the application of FASB Statements Nos. 5 & 11

11 **Illustrations of the Disclosure of "Pro Forma" Calculations**
A survey of the application of certain sections of APB Opinion Nos. 15, 16, and 20, and SAS No. 1

EMERGING PROBLEMS DIVISION

Illustrations of Accounting for Marketable Equity Securities

A survey of the application of FASB Statement No. 12

by HORTENSE GOODMAN, CPA
AND
LEONARD LORENSEN, CPA

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

NOTICE TO READERS

This is a publication of the staff of the American Institute of Certified Public Accountants and is not to be regarded as an official pronouncement of the Institute.

PREFACE

This publication is the twelfth in a series produced by the Institute's staff through use of the Institute's National Automated Accounting Research System (NAARS). The first eleven in the series are listed on the inside cover of this publication.

The purpose of the series is to provide interested readers with examples of the application of technical pronouncements. It is believed that those who are confronted with problems in the application of pronouncements can benefit from seeing how others apply them in practice.

It is the intention to periodically publish similar compilations of information of current interest dealing with aspects of financial reporting.

The examples presented were selected from over six thousand annual reports stored in the NAARS computer data base.

This compilation presents only a limited number of examples and is not intended to encompass all aspects of the application of the pronouncements covered in this survey. Individuals with special application problems not illustrated in the survey may arrange for special computer searches of the NAARS data banks by contacting the Institute.

The views expressed are solely those of the staff.

Paul Rosenfield
Director, Technical Research Division

TABLE OF CONTENTS

I

SCOPE AND PURPOSE OF THE SURVEY

DESCRIPTION OF FASB STATEMENT NO. 12

In December 1975 the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 12, "Accounting for Certain Marketable Securities." Statement No. 12 prescribed standards of accounting for marketable equity securities, including the amount at which those securities should be stated in financial statements and the manner in which gains and losses from sale or market value changes should be recognized and reported. Different treatment of gains and losses is prescribed for current and non-current securities and for temporary and permanent market value changes.

All of the recommendations of Statement No. 12 apply to enterprises in nonspecialized industries, but only some of them to enterprises in specialized industries that have developed uniform industry accounting practices for marketable securities. FASB Statement No. 12 is reproduced in Appendix A. Four Interpretations of Statement No. 12 issued by the FASB are reproduced in Appendix B.

In discussing temporary and permanent declines in market value of securities, Statement No. 12 refers to an Auditing Interpretation issued by the staff of the Auditing Standards Division of the AICPA in January 1975. The Interpretation, titled "Evidential Matter for the Carrying Amount of Marketable Securities," discusses the determination of declines in market value of marketable securities as temporary or permanent and the classification of the securities as current or noncurrent. The Interpretation is reproduced in Appendix C.

SOURCE OF ILLUSTRATIONS

Accounting for marketable equity securities in accordance with FASB Statement No. 12 requires considerable judgment. An accountant who is confronted with problems in applying the Statement can benefit from learning how other accountants have applied it in practice. Accordingly, excerpts from financial statements contained in recently published annual reports to shareholders of business enterprises are presented in this publication to illustrate application of the Statement.

The AICPA National Automated Accounting Research System (NAARS) was used to compile the information. The examples presented were selected from the published annual reports to shareholders of more than 6,000 companies stored in the computer data base.

II

ASSET PRESENTATION

FASB Statement No. 12 requires the carrying amount of a marketable equity securities portfolio to be the lower of its aggregate cost or market value, determined at the balance sheet date. The amount by which aggregate cost of the portfolio exceeds market value is to be accounted for as the valuation allowance.

The marketable equity securities owned by an entity are required, in the case of a classified balance sheet, to be grouped into separate portfolios according to the current or noncurrent classification of the securities for the purpose of comparing aggregate cost and market value to determine carrying amount. In the case of an unclassified balance sheet, marketable equity securities are considered as noncurrent assets for the purposes of the Statement.

As of the date of each balance sheet presented, Statement No. 12 requires disclosure of aggregate cost and market value (each segregated between current and noncurrent portfolios if a classified balance sheet is presented) with identification as to which is the carrying amount. The gross unrealized gains and the gross unrealized losses making up the difference between aggregate cost and market values for each portfolio are also required to be disclosed.

Twenty-eight examples of the presentation of marketable equity securities as assets in accordance with Statement No. 12 are presented. The examples are classified according to whether they pertain to current or noncurrent assets or to an unclassified balance sheet. In some examples gross unrealized gains and gross unrealized losses were not disclosed, apparently on grounds of immateriality.

CURRENT ASSETS

AMEX INC.
Consolidated Statement of Financial Position

	December 31	
Assets	1975	1974(A)
Current assets		
Cash	$ 26,920	$22,420
Time deposits and certificates of deposit	61,120	97,820
Chevron preferred shares (Note 14)	163,850	—
Marketable securities (Note 8)	17,290	23,010

• • • •

Notes to Financial Statements

8. Marketable Securities:

Marketable securities are reported at the lower of cost or market. Marketable securities include equity securities at cost of $5,180 and $21,650 in 1975 and 1974, less reductions to market value of $200 and $5,470, respectively. Realized losses of $3,780 and $360 were charged to earnings in 1975 and 1974.

HOWARD JOHNSON COMPANY

Consolidated Balance Sheet

	January 2, 1976	January 3, 1975
Assets		
Current assets:		
Cash	$ 3,822	$ 3,564
Marketable securities, at approximate market value in 1975 and at cost less a reserve of $412,000 in 1974 (Note 2)	66,218	42,992

••••

Notes to Financial Statements

Note 2—Marketable Securities

In accordance with recent authoritative pronouncements, the Company's investment in equity securities at January 2, 1976 (all of which are preferred stocks) are stated at approximate market value, which recognizes gross unrealized losses of $1,113,000 at that date. At January 3, 1975, a $412,000 reserve had been provided to recognize a decline in market value of certain equity securities. This amount has been reclassified to conform with the 1975 presentation. Market values for the aggregate portfolio were $66,290,000 and $42,100,000, respectively, at the above year-end dates.

MASCO CORPORATION

Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Current Assets:		
Cash	$ 4,266	$ 5,415
Marketable securities, at cost (approximates market)	44,332	23,924

••••

Notes to Financial Statements

Marketable Equity Securities

Included in marketable securities are equity securities having an aggregate cost of $3,402,000 and $10,258,000 and an aggregate market value of $3,985,000 and $10,479,000 at December 31, 1975 and 1974, respectively. At December 31, 1975, there were no unrealized losses on marketable equity securities.

NATIONAL CITY LINES, INC.
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Current Assets:		
Cash	$2,481	$3,576
Temporary cash investments	3,980	1,270
Marketable securities (Notes A-1 and C)	812	1,989

• • • •

Notes to Financial Statements

C. Marketable Securities:

At December 31, 1975, marketable equity securities are carried at cost, less a valuation reserve of $113,000 ($79,000 net of tax), which was provided in 1975 to reduce the carrying amount to aggregate quoted market value in accordance with the provisions of the Statement of Financial Accounting Standards No. 12. At December 31, 1975, aggregate unrealized losses of $125,000 and aggregate unrealized gains of $12,000 are included in the valuation reserve. At December 31, 1974, marketable equity securities, carried at cost less a provision for permanent market decline, had a quoted market value of $1,620,000.

• • • •

THE NEWHALL LAND AND FARMING COMPANY
Consolidated Balance Sheet

February 29, 1976 and February 28, 1975

	1976	1975
Assets		
Current assets		
Cash	$2,421	$2,184
Marketable securities (note 8)	3,878	435

• • • •

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

• • • •

Marketable Securities. The cost of securities sold is based on the average cost of all shares of each security held at the time of sale. During fiscal 1976, the Company realized gains of $364,000 on the sale of marketable equity securities.

• • • •

Note 8. Composition of Certain Financial Statement Captions

	(in thousands) 1976	1975
Marketable Securities		
Commercial paper	$3,700	
Marketable equity securities at cost (market value $806,000 and $1,255,000; the difference between cost and market is all unrealized gains)	178	$435
	$3,878	$435

• • • •

TECHNITROL, INC.
Consolidated Balance Sheets

	December 31, 1975	1974*
Assets		
Current assets:		
Cash and certificate of deposit ($300,000 in 1975)	$ 846	287
Securities (note 3)	1,192	—
Receivables (note 6):		
Trade	2,005	1,801
Affiliate	3	148
Other	82	67
Inventories (notes 4 and 6)	2,481	2,932
Prepaid expenses	178	58
Total current assets	6,787	5,293
Property, plant and equipment (note 6):		
Land	43	55
Buildings and improvements	608	640
Machinery and equipment	4,393	3,480
	5,044	4,175
Less accumulated depreciation	2,827	2,590
Net property, plant and equipment	2,217	1,585
Securities (note 3)	—	1,192
Other assets:		

• • • •

Notes to Financial Statements

(3) Securities

At December 31, 1975, securities were as follows:

	Cost	Market Value
Common stock of affiliate disposed of in January 1976	$ 228,000	555,000
Preferred stocks	964,000	695,000
	$1,192,000	1,250,000

In accordance with Statement No. 12 issued by the Financial Accounting Standards Board in December 1975, investments are carried at the lower of cost or market in 1975. Gross unrealized gains and gross unrealized losses at December 31, 1975 are as follows:

	Gains	Losses
Common stock of affiliate	$327,000	—
Preferred stocks	—	269,000

Although the Company's investment in the affiliate approximated a 15% interest (32% voting interest), the Company did not exercise significant influence over its operations since substantially all of the voting interest, other than that of the Company, was controlled by two persons. Sales to the affiliate were $665,000 in 1975 and $1,193,000 in 1974.

On January 6, 1976, the shareholders of the affiliate approved a plan of liquidation whereby all of its assets were sold. The Company received $555,000 on January 9, 1976 from this disposition and is to receive $365,000 of royalty payments through 1981, less its pro rata share of any future liquidation expenses to be incurred. In addition, if certain sales quotas are met, the Company may receive additional proceeds up to $154,000 through 1981.

At December 31, 1974, securities were as follows:

	Cost	Value*
Common stock of affiliate	$ 228,000	116,000
Preferred stocks	964,000	635,000
	$1,192,000	751,000

*Equity in underlying net assets of affiliate and market value of preferred stocks.

At December 31, 1974, investments were carried at cost and were not required to be carried at the lower of cost or market. Such investments were classified as noncurrent assets since the Company did not intend to dispose of them at that time.

YATES INDUSTRIES, INC.
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Current Assets:		
Cash (including time deposits—1975, $2,753,990; 1974, $4,586,848) (Note 6)	$4,311	$5,879
Marketable equity securities (Note 2)	92	132

• • • •

Notes to Financial Statements

2. Marketable Equity Securities

At December 31, 1975, marketable equity securities are included in current assets and are carried at the lower of cost or market. A valuation allowance in the amount of $39,805, representing the gross unrealized loss on such securities, was established by a charge to income.

Marketable equity securities held on December 31, 1974 with a market value of $78,375 were not required to be carried at the lower of cost or market and are therefore stated at cost.

NONCURRENT ASSETS

BROCKWAY GLASS COMPANY, INC.
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
• • • •		
Total current assets	91,584	77,740
Investments, at cost (Note 3)	6,240	6,240
• • • •		

Notes to Financial Statements

3. Non-Current Marketable Equity Securities

In accordance with the provisions of Financial Accounting Standards Board Statement No. 12 the following information is presented with respect to non-current marketable equity securities included in investments at December 31, 1975 and 1974.

	1975	1974
Aggregate market value	$5,460,000	$4,870,000
Aggregate cost (carrying value)	3,978,534	3,978,534
Gross unrealized gains	1,481,466	891,466
Gross unrealized losses	—	—

There were no sales of marketable equity securities in 1975 or 1974.

CAPITAL CITIES COMMUNICATIONS, INC.
Consolidated Balance Sheet

	December 31, 1975	1974
• • • •		
Total current assets	82,632	68,007
Property, Plant and Equipment, at cost		
Land and land improvements	8,587	8,513
Buildings	22,681	21,607
Broadcasting, printing and other equipment	50,200	46,711
	81,468	76,831
Less accumulated depreciation	30,573	26,051
Property, plant and equipment, net	50,895	50,780
Intangible Assets	159,593	160,396
Marketable Equity Securities, at cost	6,971	6,962
• • • •		

Notes to Financial Statements

5. Marketable Equity Securities

Marketable equity securities were carried at an aggregate cost of $6,971,000 and $6,962,000 and had an aggregate market value of $8,569,000 and $6,464,000 at December 31, 1975 and 1974, respectively. At December 31, 1975 there were aggregate unrealized gains of $1,776,000 and unrealized losses of $178,000.

DATA SYSTEMS ANALYSTS, INC.
Consolidated Balance Sheets

	Years ended December 31 1975	1974
• • • •		
Total Current Assets	1,277	1,048
Other Assets		
Marketable securities—at the lower of cost or market in 1975 (cost $33,328) and at cost in 1974 (market $20,000)—Note C	18	33
• • • •		

Notes to Financial Statements

Note C—Marketable Securities

At December 31, 1975, the Company holds marketable securities with an aggregate cost of $33,328 classified as a noncurrent asset. The composition of the portfolio is as follows:

	Cost	Market Value	Unrealized Loss
Cybermatics, Inc.	$18,328	$ 3,750	$14,578
Medical Services, Inc.	15,000	15,000*	—
	$33,328	$18,750	$14,578

*Estimated fair value as determined by management.

At December 31, 1975, the Company changed the basis for carrying its marketable equity securities from cost to lower of aggregate cost or market value. This change, required by a recent pronouncement of the Financial Accounting Standards Board, reduced shareholders' equity at December 31, 1975 by $14,578 (no tax effect) represented by the unrealized loss on marketable securities at that date. In the opinion of management, no material loss will be realized on the disposition of the securities without quoted market value at December 31, 1975.

DOW JONES & COMPANY, INC.
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
• • • •		
Total current assets	87,055	76,255
Investments in Associated Companies, at equity (Note 4)	13,092	13,287
Marketable Equity Securities (Note 5)	5,740	833
• • • •		

Notes to Financial Statements

Note 5. Marketable Equity Securities:

Marketable equity securities are carried at the lower of aggregate cost or market as of December 31, 1975, in accordance with FASB 12, and at cost as of December 31, 1974.

Market values at December 31, 1975 and 1974, were $5,857,515 and $714,936, respectively. At December 31, 1975, gross unrealized gains and losses amounted to $247,563 and $130,752, respectively.

In April 1975, the Company acquired 10% of the common stock of South China Morning Post, Limited. There were no sales of marketable equity securities during 1975 and 1974.

EMERY AIR FREIGHT CORPORATION
Statement of Consolidated Financial Position

	December 31, 1975	December 31, 1974
• • • •		
Marketable Securities Held for Investment (Note 3):		
Debt securities carried at cost	8,112	6,642
Equity securities carried at market in 1975 and at cost in 1974	2,098	2,767
	10,210	9,410
Other Assets	494	544
Net Assets	$43,672	$38,269
• • • •		

Notes to Financial Statements

Note 1—Summary of Significant Accounting Policies

• • • •

Marketable Equity Securities—In 1975, new standards were promulgated by the Financial Accounting Standards Board for accounting for marketable equity securities. The revised standards require that, for periods ending on or after December 31, 1975, marketable equity securities be carried at their lower of cost or market at the balance sheet date.

• • • •

Note 3. Marketable Securities Held for Investment

A summary of debt securities held for investment is as follows:

	December 31, 1975	December 31, 1974
Cost	$8,112,402	$6,642,930
Market	$7,916,050	$6,259,890

The decline in market value of these securities at December 31, 1975 is considered to be temporary.

To reduce the carrying amount of marketable equity securities (consisting entirely of preferred stocks) to market, which was lower than cost ($2,767,130) at December 31, 1975, a valuation allowance representing the net unrealized loss in the amount of $669,005 was established by a charge to stockholders' equity. The gross unrealized loss at December 31, 1975 was $669,005.

At December 31, 1974, marketable equity securities held for investment had a market value of $1,864,124.

GENERAL ELECTRIC COMPANY

Statement of Financial Position

	December 31 (In millions) 1975	1974	Additional information
• • • •			
Current assets	5,565.5	5,222.6	
Investments	1,050.1	1,004.8	(note 12)
Plant and equipment	2,562.4	2,615.6	(note 13)
Other assets	585.5	526.1	(note 14)
Total assets	$9,763.5	$9,369.1	
• • • •			

Notes to Financial Statements

12. Investments

	December 31 (In millions) 1975	1974
Nonconsolidated finance affiliates	$ 508.6	$ 456.5
Miscellaneous investments (at cost):		
Government and government-guaranteed securities	268.0	210.7
Other	73.7	91.2
	341.7	301.9
Marketable equity securities:		
Honeywell Inc. and Honeywell Information Systems Inc.	100.3	141.3
Other	69.2	69.3
	169.5	210.6
Associated companies	43.1	48.3
Less allowance for losses	(12.8)	(12.5)
	$1,050.1	$1,004.8

Advances to nonconsolidated finance affiliates aggregated $0.7 million at the end of 1975 and 1974.

The estimated realizable value of miscellaneous investments at December 31, 1975 was $330 million ($285 million at December 31, 1974).

Marketable equity securities were valued at the lower of cost or market at December 31, 1975 and at cost at December 31, 1974. Aggregate market value of marketable equity securities was $219 million and $191 million at year-end 1975 and 1974, respectively. At December 31, 1975 gross unrealized gains on securities in the portfolio were $64 million and gross unrealized losses were $14 million. Market value calculations include the Company's investment in Honeywell Information Systems Inc. (HIS) as being equivalent to 2,200,000 shares of Honeywell Inc. common stock. Cost of the investment in Honeywell Inc. and HIS is the appraised fair value recorded on October 1, 1970, when the General Electric information systems equipment business was transferred to HIS. The recorded value is substantially less than tax cost.

At December 31, 1975, General Electric held 380,800 shares of Honeywell common stock, compared with 1,437,716 shares at December 31, 1974. GE sold 1,056,916 shares of Honeywell common stock in 1975 and 174,716 shares in 1974. Using average cost, realized gains entering into the determination of net income were nominal in both 1975 and 1974.

General Electric held an 18½% ownership in HIS at December 31, 1975 and 1974. An Agreement between General Electric and Honeywell provides that GE can require Honeywell to purchase its interest at any time during 1976 for 1,500,000 shares of Honeywell stock, at any time during 1977 for 1,800,000 shares of Honeywell stock, and at any time during 1978 for 2,200,000 shares of Honeywell stock. In addition, under certain circumstances Honeywell has the right during the 1976-77 period to require GE to sell its HIS interest to Honeywell in return for 2,200,000 shares of Honeywell stock. During 1978 Honeywell has an unlimited right to purchase GE's HIS interest for 2,200,000 shares of Honeywell stock. Also, under the Agreement, GE may partially exercise its option rights to cause Honeywell to acquire that number of shares of HIS which will result in GE receiving 800,000 shares of Honeywell stock.

In January 1976, General Electric notified Honeywell that it had elected to exercise its partial options for a total of 800,000 Honeywell shares. Upon closing, General Electric will retain an 11.7% ownership in HIS, and GE and Honeywell will retain their options with respect to the remaining HIS shares owned by General Electric.

General Electric is committed to the U.S. Department of Justice to dispose of its year-end 1975 holding of Honeywell common stock in an orderly manner by June 30, 1978 and all other shares of Honeywell common stock that GE receives for its interest in HIS by December 1980.

A voting trust has been established in which General Electric must deposit all shares of Honeywell common stock received as part of these transactions.

• • • •

GLEN-GERY CORPORATION

Consolidated Balance Sheets

	December 31 1975	December 31 1974
• • • •		
Total Current Assets	8,120	8,372
Investments and Other Assets		
Marketable equity securities, carried at market in 1975 and at cost in 1974—Note B	228	511
Other investments and sundry assets	286	318
	514	829

• • • •

Notes to Financial Statements

Note B—Marketable Equity Securities

In conformity with the requirements of a recent Statement of the Financial Accounting Standards Board, marketable equity securities included in non-current assets at December 31, 1975, are carried at market value which is less than their cost of $511,187. A valuation allowance of $282,287 was established by a charge to Shareholders' Equity representing the net unrealized loss. The securities were not required to be carried at the lower of cost or market ($220,725) at December 31, 1974 and, accordingly, were stated at cost. There were no sales of marketable equity securities during 1975. The change in method of carrying the securities had no effect on net income or working capital.

H & R BLOCK, INC.

Consolidated Balance Sheet

	April 30 1976	April 30 1975
• • • •		
Total Current Assets	66,717	60,414
Investments and Other Assets:		
Investments in marketable securities (Notes 1 and 2)	31,009	23,001

• • • •

Notes to Financial Statements

1. Summary of Significant Accounting Policies:

• • • •

B. Marketable securities:

Both current and noncurrent marketable securities consist principally of municipal bonds and notes which are stated at amortized cost. Marketable equity securities, included in noncurrent assets, were stated at the lower of aggregate cost or market value at April 30, 1976, and at cost at April 30, 1975 (see Note 2).

• • • •

2. Marketable Securities:

In accordance with the Financial Accounting Standards Board Statement No. 12, marketable equity securities at April 30, 1976, all of which are included in noncurrent assets, are stated at the lower of their aggregate cost, $5,073,000, or market value, $4,338,000, with the resultant net unrealized loss, in the amount of $735,000 (representing unrealized gains of $85,000 and unrealized losses of $820,000), being reflected as a charge to stockholders' equity. The remainder of the noncurrent marketable securities at April 30, 1976 are stated at amortized cost, $26,671,000, which approximated their market value at that date, $26,698,000. At April 30, 1975, marketable equity securities were not required to be carried at the lower of their aggregate cost or market value, and all marketable securities were stated at amortized cost; the cost of the marketable equity securities at that date, $4,785,000, exceeded their market value by $1,391,000. The cost of the remainder of the noncurrent marketable securities at April 30, 1975, $18,216,000, exceeded their market value by $564,000.

The cost of marketable securities classified as current assets at both April 30, 1976 and 1975 approximated their market value.

During 1975, the Company reclassified certain of its investments in marketable securities from current to noncurrent assets in accordance with managements' intention to hold such securities beyond one year.

HECLA MINING COMPANY

Consolidated Balance Sheets

	December 31, 1975	December 31, 1974
••••		
Total current assets	22,151	14,363
Investments and interests in mining properties:		
Granduc Mines, Limited (N.P.L.) (Note 6)	6,769	7,830
Marketable equity securities, carried at market in 1975 and at cost in 1974 (Note 4)	2,525	2,944
••••		

Notes to Financial Statements

1. Summary of Significant Accounting Policies:

••••

Investments—The Company follows the equity method of accounting for investment in common stock of companies 20% to 50% owned. Marketable equity securities are carried at market in 1975 and at cost in 1974. Other investments not intended for resale or not readily marketable are included in other investments at cost.

••••

4. Marketable Equity Securities:

In accordance with Statement No. 12 of the Financial Accounting Standards Board, the noncurrent portfolio of marketable equity securities is carried at the lower of cost or market at December 31, 1975. Marketable equity securities at December 31, 1975 consisted of the following:

	Cost	Market	Unrealized Gain or (Loss)
Sunshine Mining Company 3.7% owned	$2,574,087	$2,111,910	$(462,177)
Rosario Resources Corp.	203,890	413,712	209,822
	$2,777,977	$2,525,622	$(252,355)

To reduce the carrying amount of the non-current marketable equity securities portfolio to market, which was lower than cost at December 31, 1975, a valuation allowance in the amount of $252,355 was established by charge to shareholders' equity representing the net unrealized loss.

At December 31, 1974, the non-current portfolio of marketable equity securities was not required to be carried at lower of cost or market at the balance sheet date and was carried at cost. Marketable equity securities included in non-current assets had a market value of $2,670,599 at December 31, 1974.

••••

KANSAS CITY SOUTHERN INDUSTRIES, INC.
Consolidated Balance Sheets

	December 31, 1975	December 31, 1974 (Note 9)
Assets		
••••		
Total Current Assets	39,105	37,955
Investments:		
Held for operating purposes	4,143	4,074
Marketable equity securities (Notes 2 and 9)	5,457	5,756

••••

Notes to Financial Statements

Note 1—Accounting Policies:

••••

Investments: Short-term investments included in current assets are stated at cost which approximates market.

Noncurrent investments in operating companies 20% or more owned are accounted for under the equity method; other investments held for operating purposes are stated at cost. Marketable equity securities are stated at the lower of aggregate cost or market. The Company uses the average cost basis in computing gain or loss on sale of marketable equity securities. Other noncurrent investments are stated at cost which approximates market.

••••

Note 2—Marketable Equity Securities:

Marketable equity securities are stated at cost (which is less than aggregate market value) as follows:

	December 31, 1975	December 31, 1974
	(In Thousands)	
Market value	$19,101	$15,611
Cost	5,457	5,756
Excess of market value over cost	$13,644	$ 9,855

The excess of market value over cost reflects gross unrealized gains of $13,691,000 ($10,300,000 in 1974) less gross unrealized losses of $47,000 ($445,000 in 1974).

••••

Note 9—Prior Year Restatement:

During fiscal 1971 the Company became one of several defendants in four separate derivative actions brought on behalf of four mutual funds which have investment advisory and underwriting agreements with Supervised Investors Services, Inc. (SIS), and in a direct action brought by the mutual funds. All of these actions arose out of the 1970 merger of SIS, in which the Company had an investment, into Kemperco, Inc. and sought to recover profits allegedly realized by the defendants in the "sale" of their investment in SIS to Kemperco. A stipulation of settlement was entered into by the parties to these actions which was approved by the United States District Court for the Northern District of Illinois in fiscal 1975. The settlement provided for payment by all defendants of a gross sum of $1,400,000 including the Company's portion, $1,085,000, which was paid in October 1975. Such payment represents additional cost basis of the Company's investment in Kemperco (formerly SIS). Since half of such investment was sold in 1971, retained earnings have been restated to reflect a retroactive reduction of $543,000 in the gain on such sale ($.32 per share); the remaining $542,000 has been accounted for retroactively as additional investment in shares of Kemperco common stock still owned by the Company at December 31, 1975.

LEASEWAY TRANSPORTATION CORP.
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Current assets		
Cash, including certificates of deposit of $11,660,000 and $5,250,000	$ 19,518	$18,785
Short-term investments—at cost (approximates market)	36,252	13,267
Notes and accounts receivable, less allowance of $850,000 and $475,000	41,668	41,545
Federal income tax refund	378	674
Inventory of parts and supplies	5,151	9,131
Prepaid licenses, insurance and other	5,299	5,340
	108,268	88,744
Investments in Securities (Note 2)		
Securities carried at cost (quoted market value $15,900,000 and $8,900,000)	17,864	11,678
Securities carried at market in 1975 and at cost in 1974 (cost in 1975 of $19,808,000; market in 1974 of $16,900,000)	16,508	24,262
	34,372	35,941

Notes to Financial Statements

2. Investments in Securities

Securities Carried at Cost. These securities consist of sinking fund preferred stocks of listed companies, which are redeemable in the future by the issuers at aggregate amounts in excess of their cost. No provision has been made for the decline in market value as the Company has no present intention of disposing of the securities and believes that the amount realized on the eventual redemption or other disposition of the securities will exceed their cost.

Securities Carried at Market in 1975 and at Cost in 1974. These securities consist of preferred and convertible preferred stocks of listed companies. In 1974 these securities also included common stock of a listed company.

The Financial Accounting Standards Board (FASB) issued a pronouncement in December 1975 requiring that "marketable equity securities" be carried at the lower of their aggregate cost or market value. The pronouncement also provides that a valuation allowance (reducing the carrying value to market) be established by a charge to stockholders' equity. These securities are "marketable equity securities" as that term is defined by the FASB. Accordingly, the method of valuation of these securities was changed to market value, which was lower than cost at December 31, 1975. The change did not affect net earnings for the year.

The valuation allowance of $3,300,000 at December 31, 1975 provides for unrealized losses of $3,343,000 offset by unrealized gains of $43,000. During 1975, realized net losses of $80,000 from the sale of these securities were deducted in determining net earnings. The cost of securities sold was determined using the first-in, first-out method.

• • • •

MURPHY OIL CORPORATION
Consolidated Balance Sheets

	December 31 1975	December 31 1974
• • • •		
Total current assets	413,412	370,627
Investments in unconsolidated subsidiaries and jointly owned companies	76,306	45,980
Other investments	19,621	21,595
• • • •		

Notes to Financial Statements

Other Investments—Included in other investments at December 31, 1975 are marketable equity securities having a cost and a market value of $7,155,000 and $10,799,000, respectively. Gross unrealized gains amounted to $3,644,000. There were no gross unrealized losses.

PATO CONSOLIDATED GOLD DREDGING LIMITED

Balance Sheets

	December 31, 1975	1974*
••••		
Total current assets	15,713	10,692
Marketable securities, 1975 at lower of cost or market, 1974 at cost (market $2,578,000)	9,678	5,399
••••		

Notes to Financial Statements

Note 1—Summary of Significant Accounting Policies

••••

Marketable Securities

Noncurrent marketable equity securities are carried at the lower of aggregate average cost or aggregate market value at December 31, 1975. The amount by which the aggregate cost of noncurrent marketable equity securities exceeds the aggregate market value together with the Company's share of a similar provision recorded by its Brazilian affiliate is recorded as a reduction of shareholders' equity. At December 31, 1974, marketable securities were carried in the balance sheet at cost less a reserve.

••••

Note 2—Accounting Changes

••••

During 1975, the Company and CBMM also adopted Financial Accounting Standard No. 12 "Accounting for Certain Marketable Equity Securities." The effect of this change in 1975 is to reduce the Company's carrying value of its marketable equity securities by $3,877,673 and to reduce its investment in CBMM by $839,869.

Note 4—Marketable Securities

The noncurrent portfolio of marketable securities at December 31, 1975 comprises the following:

Companies	Number of Shares	Cost	Quoted Market Value
Inspiration Consolidated Copper Company	87,900	$ 2,508,861	$1,853,837
Kawecki Berylco Industries, Inc.	163,759	2,421,436	1,165,113
United Brands Company	421,100	2,292,390	2,247,032
Wyman-Gordon Company	47,215	1,667,404	1,487,669
RLC Corp	126,900	1,398,113	644,906
Ex-Cell-O Corporation	35,400	1,166,991	508,225
Molycorp, Inc.	48,600	844,133	889,147
Chicago, Rock Island and Pacific Railroad Company	129,700	648,500	329,568
Other		608,375	553,033
		$13,556,203	$9,678,530

A valuation allowance of $3,877,673 was established by a charge to shareholders' equity to reduce the carrying amount of the noncurrent marketable equity portfolio to the lower of aggregate cost or market at December 31, 1975. The gross unrealized gains and gross unrealized losses included in the valuation reserve were $45,565 and $3,923,238, respectively.

At December 31, 1974, marketable equity securities were carried at cost except for Chicago, Rock Island and Pacific Railroad Company for which investment a provision for possible loss of $1,507,000 was charged to continuing operations.

The noncurrent portfolio has been pledged as collateral to secure the bank loan at December 31, 1975.

THE SPERRY AND HUTCHINSON COMPANY

Consolidated Balance Sheet

	January 3, 1976	December 28, 1974
••••		
Total current assets	282,463	290,498
Investments in marketable securities (Note 1):		
Debt obligations (at cost)	37,249	41,487
Equity securities (at market in 1975; at cost in 1974)	26,125	34,692
••••		

Notes to Financial Statements

1. Investments in Marketable Securities

	1975			1974		
	Cost	Quoted market value	Depreciation	Cost	Quoted market value	Depreciation
Investments classified as current assets						
Debt obligations	$19,520	$19,478	$ 42	$11,140	$11,084	$ 56
Accrued interest receivable	671	671		882	882	
	$20,191	$20,149	$ 42	$12,022	$11,966	$ 56
Investments classified as non current assets						
Debt obligations, maturing beyond one year	$37,249	$34,807	$2,442	$41,487	$38,968	$ 2,519
Equity securities:						
Common stock	$23,087	$15,592	$7,495	$23,785	$12,164	$11,621
Preferred stock	12,932	10,533	2,399	10,907	7,590	3,317
	36,019	26,125	$9,894	34,692	19,754	14,938
Less allowance for valuation of marketable equity securities	9,894*					
	$26,125	$26,125		$34,692	$19,754	$14,938

*Excludes allowance of $194 applicable to equity investments of an unconsolidated subsidiary.

Depreciation in marketable equity securities at January 3, 1976 is net of appreciation of $788. Reference should also be made to the summary of significant accounting policies regarding investments in marketable securities. As of February 27, 1976, equity security investments amounted to $35,707 and the quoted market value was $28,213.

Summary of Significant Accounting Policies

••••

Investments in marketable securities

The Company regards its investments in marketable securities as part of its long range investment policy. Consistent with this policy, the Company invests primarily in bonds which are generally held to maturity, amortizes bond premium and accrues interest earned. The balance of the investments are made in preferred and common stocks which the Company believes will afford a satisfactory long-term return. Accordingly, all investments in marketable securities, other than obligations maturing within one year, are classified as non current assets in the accompanying financial statements.

Prior to the year ended January 3, 1976, the Company carried all investments at cost. However, as of that date and in accordance with Financial Accounting Standards Board Statement No. 12 issued in December, 1975, marketable equity securities, which are all classified as non current assets, are carried at the lower of aggregate cost or market. The amount by which the market value is less than cost is accounted for as an allowance for valuation of marketable equity securities and changes in the allowance are made directly to stockholders' equity.

Where the Company determines that in its opinion there is a permanent impairment in value, the securities are sold and the loss recognized and charged to operations. The Company also disposes of securities when more favorable investment opportunities become apparent. The cost of securities for determining gain or loss on the sale of securities is determined principally on the first-in, first-out method.

••••

UNION PACIFIC CORPORATION
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974 (As Restated)
••••		
Total current assets	460,182	347,736
Investments (Note 2)		
Investments in affiliated companies	68,564	56,761
Other investments	61,107	61,153

••••

Notes to Financial Statements

2. Investments

Investments in affiliates are carried at equity. Net income for the years ended December 31, 1975 and 1974 includes equity in net income of affiliates of $5,943,000 and $1,821,000, respectively.

Other investments at December 31, 1975 and 1974 include $46,791,000 of marketable equity securities carried at written down cost. At December 31, 1975, the carrying value for such securities approximated quoted market value with no significant gross unrealized gains or losses; whereas, at December 31, 1974, quoted market value was approximately $14,672,000 less than written down cost.

Marketable equity securities include an investment in 2,149,319 shares of I.C. Industries, Inc. (formerly Illinois Central Industries, Inc.) common stock with a carrying value of $35,195,000 at December 31, 1975. The Corporation has agreed to dispose of the entire investment by 1982. Under a plan of divestiture one-third of the stock is to be sold by the end of 1976; however, the Corporation has retained the right to amend the plan of divestiture depending upon several factors, including market conditions.

CURRENT AND NONCURRENT ASSETS

CRYSTAL OIL COMPANY
Consolidated Balance Sheet

	December 31 1975	December 31 1974
Assets		
Current Assets		
Cash (including U.S. Government securities of $3,500,000 in 1975 and certificates of deposit of $1,510,000 in 1974)	$ 4,996	$ 3,985
Marketable securities—at cost—Note C		
AMAX, Inc. Cumulative Preferred Stock—market value $4,500,000	3,617	—
Receivables—Note C		
Trade accounts, less allowances of $239,000 in 1975 and $438,000 in 1974	11,534	13,336
Notes	557	537
Crude oil, refined products and other inventories—Note C	4,410	6,272
Prepaid expenses and other current assets	843	755
Total Current Assets	25,957	24,885
Investments—at cost—Note C		
AMAX, Inc. Cumulative Preferred Stock—market value $3,930,000 in 1975 and $8,061,000 in 1974	3,160	9,168
Other stocks	840	834
Total Investments	4,000	10,002

••••

Notes to Financial Statements

Note C—Mortgage and other notes

• • • •

Substantially all property, plant and equipment (excluding mine properties) is mortgaged as collateral to the mortgage notes. AMAX stock and other investments ($7,489,000), inventories ($736,000) and notes and accounts receivable ($1,912,000) are also pledged as collateral on the mortgage notes and other notes.

An amount equal to one-half of the carrying value of the AMAX, Inc. stock classified as current assets has been reclassified from mortgage and other notes to current installments on long-term debt in accordance with a provision of the mortgage note to a bank.

• • • •

W. R. GRACE & CO.

Consolidated Balance Sheet

	December 31 1975	1974
Assets		
Current Assets		
Cash, including time deposits of $26,816 (1974—$40,607)	$ 55,644	$ 72,753
Common stock subscribed	104,000	—
Marketable securities	46,498	87,233
Notes and accounts receivable:		
Trade, less allowances of $13,717 (1974—$15,221)	419,406	450,193
Other, less allowances of $2,927 (1974—$2,107)	63,075	62,926
Inventories	576,293	678,254
Prepaid expenses	31,423	34,896
Total Current Assets	1,296,339	1,386,255
Other Assets		
Investments:		
Partnerships	16,622	—
Less than majority owned companies	46,355	44,346
Occidental Petroleum Corporation	17,500	17,500
Long term receivables and other assets	102,666	96,104
Goodwill, less amortization of $14,392 (1974—$13,998)	81,051	91,378
Total Other Assets	264,194	249,328

• • • •

Notes to Financial Statements

Note 6—Marketable Securities:

Current marketable securities are carried at cost which approximates market except that equity securities at a cost of $17,532 (1974—$23,767) have been reduced by a valuation reserve of $3,037 (1974—$6,900) to adjust their carrying value to approximate market. The noncurrent portfolio of marketable equity securities is included in noncurrent assets at a cost of $9,579 which is lower than aggregate market (1974—at cost $7,458).

Net gains realized on the sale of marketable equity securities were $604 (1974—None). Aggregate unrealized gains and losses related to marketable equity securities in the portfolios at December 31, 1975, are as follows:

	Gains	Losses
Current	$ —	$3,037
Noncurrent	$11,253	$3,422

THE WILLIAMS COMPANIES

Consolidated Balance Sheet

	December 31, 1975	1974
Assets		
Current Assets:		
Cash	$ 14,042	$ 12,493
Certificates of deposit, short-term investments and marketable securities (Note 6)	48,966	73,157
Notes and accounts receivable	119,700	130,993
Contract costs and recognized income not yet billed	—	10,311
Inventories (Note 7)	180,316	150,763
Prepaid expenses	7,497	10,126
Total current assets	370,521	387,843
Investments:		
Long-term notes receivable	53,310	3,591
Preferred stocks and unregistered securities (Note 6)	57,085	52,041

● ● ● ●

Notes to Financial Statements

Note 1. Summary of significant accounting policies

● ● ● ●

Investments—At December 31, 1975, current and noncurrent portfolios of marketable equity securities are each carried at their lower of cost or aggregate market. Changes in the valuation allowance to reduce the carrying amount of current marketable equity securities to market are reflected in income while similar changes relating to noncurrent securities are shown in stockholders' equity. At December 31, 1974, such portfolios were carried at cost less an allowance for unrealized losses on the current portfolio. Other investments, including those carried in current assets, are carried at cost. Interest and dividends are reported on the accrual basis. Realized gain or loss is recognized based on first-in, first-out cost upon disposition of securities.

● ● ● ●

Note 6. Marketable equity securities

Following is a comparison of the cost, carrying value and market value of marketable equity securities included in current and noncurrent investments:

	1975	1974
Current assets:		
Cost	$ 6,365,00	$37,949,000
Allowance for unrealized loss	—	5,000,000
Carrying value	$ 6,365,000	$32,949,000
Market value	$ 7,064,000	$29,551,000
Noncurrent assets:		
Cost	$41,822,000	$41,891,000
Allowance for unrealized loss	9,963,000	—
Carrying value	$31,859,000	$41,891,000
Market value	$31,859,000	$26,359,000

At January 31, 1976, the market value of noncurrent marketable equity securities had increased by approximately $4,200,000.

At December 31, 1975, gross unrealized gains and gross unrealized losses pertaining to marketable equity securities were as follows:

	Gains	Losses
Current	$1,063,000	$ 364,000
Noncurrent	$ 114,000	$10,077,000

The valuation allowance to reduce the carrying amount of noncurrent marketable equity securities to market at December 31, 1975 resulted in a $7,794,000 charge (net of income tax benefits) to stockholders' equity.

Investment income includes net realized losses on marketable equity securities of $2,707,000 in 1975 and $10,907,000 in 1974. In 1974 an increase in the allowance for unrealized losses in current marketable securities of $4,000,000 was charged to income. In 1975, such securities were sold and the $5,000,000 of previously provided allowance was restored to income.

UNCLASSIFIED BALANCE SHEET

AVEMCO CORPORATION
Consolidated Balance Sheets

	December 31	
	1975	1974
Assets		
••••		
Investments, partially pledged, at cost, (except equity securities which are at market in 1975 and at cost in 1974) (note 4):		
Debt securities (market $6,843,217 in 1975)	7,096	4,221
Preferred stocks (cost $9,050,305 in 1975)	6,423	9,072
Common stocks (cost $5,831,489 in 1975)	5,084	6,392
Real estate	893	910
Total investments	19,498	20,596
••••		

Notes to Financial Statements

(4) Investments in Equity Securities

The following is a summary of the cost, unrealized gains and losses and estimated market values of investments in equity securities at December 31, 1975 and 1974:

	Cost	Unrealized Gains	Unrealized Losses	Estimated market values
December 31, 1975:				
Preferred stocks	$ 9,050,305	1,025	2,628,278	6,423,052
Common stocks	5,831,489	194,263	940,766	5,084,986
Total	$14,881,794	195,288	3,569,044	11,508,038
December 31, 1974:				
Preferred stocks	$ 9,072,721	—	3,644,340	5,428,381
Common stocks	6,392,254	134,252	1,893,190	4,633,316
Total	$15,464,975	134,252	5,537,530	10,061,697

Below are the amounts of unrealized increases or (decreases) in estimated market values for the years 1975 and 1974:

	1975	1974
Preferred stocks	$1,013,814	(2,677,510)
Common stocks	1,027,592	(1,392,859)
Total	$2,041,406	(4,070,369)

At December 31, 1974, the portfolio of equity securities was not required to be carried at the lower of cost or market and was carried at cost. To reduce the carrying amount of equity securities to market, which was lower than cost at December 31, 1975, as required by Statement Number 12 of the Financial Accounting Standards Board issued in December 1975, a valuation allowance in the amount of $3,373,756 was established. A corresponding charge was made to stockholders' equity representing the net unrealized loss.

Management of the Company is of the opinion that the unrealized market depreciation in investment equity securities does not include any permanent impairment of these securities when viewed as long-term investments. The Company does not plan nor does it anticipate that it will need to liquidate any securities except upon maturity or as may become desirable when market conditions become more favorable.

• • • •

AMERICAN EXPRESS COMPANY

Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Cash and due from banks	$ 421,623	$ 402,929
Time deposits	833,343	448,715
Investment securities—at cost (note 1):		
U.S. Government obligations	385,189	290,784
U.S. Government agencies' obligations	50,730	74,092
State and municipal obligations	2,017,644	1,945,638
Other bonds and obligations	655,010	503,900
Preferred stocks	36,831	133,069
Common stocks	—	51,393
Total (market: 1975, $2,751,792,000; 1974, $2,525,458,000)	3,145,404	2,998,876
Investment securities—at lower of cost or market (note 1):		
Preferred stocks	77,918	—
Common stocks	49,861	—
Total (cost: 1975, $161,774,000)	127,779	—
Investment securities—at market (note 1):		
Preferred stocks	44,692	29,643
Common stocks	409,227	322,691
Total (cost: 1975, $339,761,000; 1974, $329,218,000)	453,919	352,334

Notes to Financial Statements

1. Summary of Significant Accounting Policies

• • • •

Investment Securities

Investment securities other than stocks are carried at cost adjusted for amortization of bond discount or premium. All preferred and common stocks of the insurance subsidiaries are carried at market. At December 31, 1974, all other preferred and common stocks are carried at cost, while at December 31, 1975, in compliance with the Financial Accounting Standard No. 12, all such stocks are carried at the lower of aggregate cost or market, except that preferred stocks which either must be redeemed by the issuer or which are redeemable at the option of the holder are carried at cost. Unrealized gains and losses relating to stocks carried at market and the lower of aggregate cost or market are reflected in shareholders' equity at December 31, 1975 as follows (in millions of dollars):

	Unrealized		
	Gains	Losses	Net
Securities carried at market	$157.4	$(43.2)	$114.2
Securities carried at the lower of aggregate cost or market	7.6	(41.6)	(34.0)
			80.2
Less deferred income taxes			24.1
Net unrealized gains			$ 56.1

Net unrealized gains increased $39,399,000 during 1975 and decreased $98,038,000 during 1974. Realized gains or losses resulting from sales of investment securities represent the difference between the net proceeds and the specific amortized or original cost of the securities sold.

• • • •

WESCO FINANCIAL CORPORATION

Consolidated Balance Sheets

	December 31 1975	December 31 1974
Assets		
Cash	$ 3,584	1,067
Marketable securities (notes 3 and 11)		
Certificates of deposit	40	24,010
United States Government and agency obligations and other marketable securities, at amortized identified cost (quoted market, $48,923,000 in 1975 and $9,953,000 in 1974)	48,734	10,009
Investment in common stocks (quoted market, $1,567,000 in 1975 and $3,039,000 in 1974)	1,853	5,079
Investment in preferred stocks (quoted market, $23,825,000 in 1975 and $11,831,000 in 1974)	23,206	12,900

● ● ● ●

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

● ● ● ●

Marketable Securities

U. S. Government, agency obligations and other marketable securities are carried at identified cost, adjusted for amortization of premium and accretion of discount over the term of the security and are not carried at the lower of cost or market because it is management's intention to hold them to maturity.

Common and preferred stocks are carried at identified cost. See Note 11 for discussion of marketable equity securities.

● ● ● ●

(11) Marketable Equity Securities

The investment in marketable equity securities consists of common stocks of $1,853,000 and preferred stocks of $10,500,000, at cost. At December 31, 1975 the difference between cost and market value representing unrealized gains or losses is not material.

III

GAINS AND LOSSES PRESENTATION

Companies included in NAARS presented in recently published financial statements gains and losses as a result of (1) selling marketable equity securities during the current period, (2) establishing valuation allowances for securities, and (3) assigning a new cost basis to securities. The examples selected are in apparent conformity with FASB Statement No. 12.

SALES OF SECURITIES

Statement No. 12 describes the difference between the net proceeds from the sale of a marketable equity security and its cost as a realized gain or loss. Realized gains and losses from the sale of marketable equity securities are to be included in the determination of net income of the period in which the sales occur. For each period in which an income statement is presented, the Statement requires disclosure of the net realized gain or loss from sales included in the determination of net income and of the basis on which cost was determined in computing realized gain or loss (i.e., average cost or other method used).

Eleven examples of the disclosure of realized gains or losses from the sale of marketable equity securities are presented.

ALEXANDER & BALDWIN, INC.
Notes to Financial Statements

10. Revenues

Revenues include the following net gains:

	1975	1974
Sales of securities	$ 8,909,000	$ 471,000
Sales of real estate, other than condemnation gains	4,376,000	70,000
Condemnation gains	7,000	935,000
Total	$13,292,000	$1,476,000

See pages 3, 18 and 21 for information on significant gains included in 1975 amounts.

Page 3—To Our Stockholders

• • • •

In May and June of 1975, we sold most of our portfolio of marketable common stocks in other companies. The cost of these securities was $19,879,000 as of April 30, 1975. Between December 31, 1974 and April 30, 1975, the market value of the portfolio rose $9,107,000, or 41 percent, to $31,171,000. The sale of most of these securities resulted in capital gains that contributed $6,134,000, or 67 cents a share, to 1975 net income.

Not all of this amount can be considered unusual income, since the company has earned varying lesser amounts from sales of portfolio stocks for many years. It is the amount of the gain that is unusual, as well as the discontinuance of portfolio management as an A&B activity.

Several years ago, the A&B Board of Directors concluded that the management of a stock portfolio was a less desirable use of the company's resources than investments in operations. Accordingly, when the opportunity came to realize a major gain on the portfolio, we sold all but a few stocks and invested the proceeds in various short-term securities.

• • • •

ALLEGHANY CORPORATION

Consolidated Statements of Earnings

	Years Ended December 31, 1975	1974
Revenues from operations	$170,606	$ 84,604
Cost of operations	143,348	78,913
Gross profit	27,257	5,691
Selling, general and administrative expenses	14,861	4,925
Operating income	12,396	765
Other income (deductions):		
Gain on sales of securities (note 2)	6,268	28,199

• • • •

Consolidated Statements of Retained Earnings

Years Ended December 31, 1975 and 1974

	1975	1974
Balance at beginning of year	$46,913	$ 6,550
Net increase of equity in the prior years' earnings of Investors Diversified Services, Inc. arising from its capital transactions	—	344
Net earnings	6,079	43,540
	52,993	50,435
Less dividends declared and paid on common stock $.50 per share in 1975 and $.45 per share in 1974)	3,916	3,522
Balance at end of year	$49,076	$46,913

Notes to Financial Statements

(2) Business Changes:

• • • •

(b) Sale of Missouri Pacific Railroad Company Stock:

On January 21, 1974, an agreement with Missouri Pacific Railroad Company ("MoPac") and its parent, Mississippi River Corporation ("MRC") was consummated, settling litigation commenced in 1967 in which the Corporation sought to require the payment of reasonable dividends on the Class B stock of MoPac. Pursuant to the terms of the settlement, MoPac was recapitalized and each share of its Class A capital stock (2,200 of which were held by the Corporation) was converted into one share of a new $5 cumulative, no par, preferred stock which is convertible into one share of new common stock after December 14, 1974, and each share of its Class B capital stock (21,243 of which were held by the Corporation) received $850 in cash and sixteen shares of new common stock. The Corporation immediately sold 243,623 of its 339,888 shares of new common stock at $100 per share pursuant to a tender offer made by MRC as part of the settlement agreement.

As a result of the foregoing transactions, the Corporation received cash totalling $42,418,850, of which $18,056,550 was recorded as dividend income and $22,931,865 as gain on sales of securities. The Corporation sold the remainder of its holdings in January, 1975 for a pre-tax gain of $5,138,316.

(c) Sale of USM Corporation Stock:

On July 10, 1974, the Corporation sold its holdings of USM Corporation ("USM") common stock for cash and notes aggregating $30,464,374, recording a gain (after deducting a return to USM of "short-swing" profits of $1,191,018 pursuant to Federal securities laws) of $5,807,528 on the transaction.

• • • •

GENERAL ELECTRIC COMPANY

Notes to Financial Statements

12. Investments

• • • •

At December 31, 1975, General Electric held 380,800 shares of Honeywell common stock, compared with 1,437,716 shares at December 31, 1974. GE sold 1,056,916 shares of Honeywell common stock in 1975 and 174,716 shares in 1974. Using average cost, realized gains entering into the determination of net income were nominal in both 1975 and 1974.

• • • •

HECLA MINING COMPANY

Consolidated Statements of Income

	For the years ended December 31, 1975	1974
Income:		
Sale of concentrate and products	$29,282	$28,917
Gain on sale of securities	348	713

Notes to Financial Statements

4. Marketable Equity Securities:

• • • •

The cost of securities sold is based on the average cost of all the shares of such security held at the time of sale.

LEASEWAY TRANSPORTATION CORP.

Notes to Financial Statements

2. Investments in Securities

• • • •

Securities carried at market in 1975 and at cost in 1974.

• • • •

The valuation allowance of $3,300,000 at December 31, 1975 provides for unrealized losses of $3,343,000 offset by unrealized gains of $43,000. During 1975, realized net losses of $80,000 from the sale of these securities were deducted in determining net earnings. The cost of securities sold was determined using the first-in, first-out method.

• • • •

THE NEWHALL LAND AND FARMING COMPANY

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

• • • •

Marketable Securities. The cost of securities sold is based on the average cost of all shares of each security held at the time of sale. During fiscal 1976, the Company realized gains of $364,000 on the sale of marketable equity securities.

• • • •

UV INDUSTRIES, INC.
Notes to Financial Statements

3. Marketable Equity Securities:

• • • •

A net realized loss of $299,000 on the sale of marketable equity securities was included in the determination of net income for 1975. The cost of the securities was based on the average cost of all units held at the time of sales. There were no sales of marketable equity securities during 1974.

• • • •

WESCO FINANCIAL CORPORATION
Consolidated Statements of Earnings

	Years ended December 31, 1975	1974
• • • •		
Rental of office premises, net	288	206
Net losses on sales of marketable securities	(62)	(429)
Other income, net	32	96
• • • •		

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

• • • •

Marketable Securities

• • • •

Common and preferred stocks are carried at identified cost.

• • • •

THE E.F. MAC DONALD COMPANY
Consolidated Statements of Earnings

Years ended February 1, 1976 and February 2, 1975

	1976	1975
Net sales	$123,899	$132,026
Cost of sales	92,737	102,148
Gross profit	31,162	29,877
Operating expenses	24,977	27,348
Operating profit	6,184	2,529
Other income (expense)		
Interest and dividend income	1,256	1,366
Rental income—net	387	347
Realized gain on sale of securities	23	91
• • • •		

Notes to Financial Statements

Note B—Marketable Equity Securities

• • • •

Net realized gains of $23,298 and $91,686 on the sale of marketable equity securities were included in the determination of net earnings for fiscal years ending in 1976 and 1975, respectively. The cost of the securities sold was based on specific identification of the shares.

• • • •

SKELLY OIL COMPANY
Consolidated Statement of Income

	Years ended December 31, 1975	1974
Revenue:		
Sales, including excise taxes, and other operating revenue	$1,106,686	$985,010
Dividends, interest, and other income	14,485	11,968
Gain (loss) on securities	3,290	(5,147)
	1,124,461	991,831

● ● ● ●

Notes to Financial Statements

Note 1—Summary of Significant Accounting Policies

● ● ● ●

Marketable Securities

● ● ● ●

Included in the Statement of Income caption Gain (Loss) on Securities is a net realized loss on the disposition of marketable equity securities of $289,000 and $3,473,000 in 1975 and 1974, respectively. Also included in this caption is income resulting from the decreases in the marketable equity securities valuation allowance of $2,120,000 and $2,000 in 1975 and 1974, respectively. In determining the realized loss, the cost of the securities sold was based on the average cost of all the shares of each such security held at the time of sale.

THE WILLIAMS COMPANIES
Consolidated Statement of Income

	Years ended December 31, 1975	1974*
Income:		
Sales and services revenue	$881,899	$828,199
Investment income	14,892	346

● ● ● ●

Notes to Financial Statements

Note 1
Summary of significant accounting policies

● ● ● ●

Investments—At December 31, 1975, current and noncurrent portfolios of marketable equity securities are each carried at their lower of cost or aggregate market. Changes in the valuation allowance to reduce the carrying amount of current marketable equity securities to market are reflected in income while similar changes relating to noncurrent securities are shown in stockholders' equity. At December 31, 1974, such portfolios were carried at cost less an allowance for unrealized losses on the current portfolio. Other investments, including those carried in current assets, are carried at cost. Interest and dividends are reported on the accrual basis. Realized gain or loss is recognized based on first-in, first-out cost upon disposition of securities.

● ● ● ●

Note 6
Marketable equity securities

● ● ● ●

Investment income includes net realized losses on marketable equity securities of $2,707,000 in 1975 and $10,907,000 in 1974. In 1974 an increase in the allowance for unrealized losses in current marketable securities of $4,000,000 was charged to income. In 1975, such securities were sold and the $5,000,000 of previously provided allowance was restored to income.

ESTABLISHING VALUATION ALLOWANCES

If initial application of Statement No. 12 necessitates establishment of a valuation allowance for a marketable equity securities portfolio included in current assets, the amount thereof is required to be included in the determination of net income for the period in which the Statement is applied initially. If a valuation allowance is established for a portfolio included in noncurrent assets or in an unclassified balance sheet, the amount thereof is required to be presented separately in stockholders' equity as of the end of the period in which the Statement is applied initially.

Eighteen examples of the establishment of valuation allowances for marketable equity securities in apparent conformity with Statement No. 12 are presented. The examples are classified according to whether they pertain to current or noncurrent assets or to unclassified balance sheets.

CURRENT ASSETS

BURLINGTON NORTHERN INC.
Notes to Financial Statements

3. Short-Term Investments

• • • •

At December 31, 1975, in accordance with the requirements of FASB Statement of Financial Accounting Standards No. 12 issued in December 1975, marketable equity securities, all of which are classified as current, are carried at the lower of cost or market. To reduce the December 31, 1975 carrying value of such securities to market, a valuation allowance of $748,000 was established and charged to income at that date. Other short-term investments are stated at cost which approximates market value.

At December 31, 1974, marketable equity securities were classified as non-current and were not required to be carried at the lower of cost or market. Such securities, included primarily in Capital and Other Special Funds, were stated at cost, $4,844,000, which exceeded market value by approximately $1,849,000.

10. Other Income (Charges)

Included in Other income (charges)—net were the following related to the Company's investments in securities (based on specific investment cost):

	(In Thousands of Dollars) 1975	1974
Marketable equity securities:		
Reduce carrying value to market (Note 3)	$ (748)	
Net realized gain (loss)	21	$ (31)
Net realized gain on disposition of other investments	3,188	522
Allowance for possible losses and write-offs of other investments	(45)	(3,289)
Total	$2,416	$(2,798)

DILLINGHAM CORPORATION
Consolidated Statements of Earnings

	Years ended December 31, 1975	1974
• • • •		
Other income (expense):		
Interest	4,936	5,117
Gain on sale of property and equipment	7,896	7,693
Provision for decline in value of marketable equity securities	(1,481)	—
Other income (expense), net	(1,742)	3,710

• • • •

Notes to Financial Statements

Summary of Significant Accounting Policies

• • • •

Marketable Securities

Marketable securities valued at $993,000 are included in other current assets at December 31, 1975. In accordance with Statement No. 12 of the Financial Accounting Standards Board, a valuation allowance in the amount of $1,481,000 was established to reduce the cost basis of $2,474,000 to market, with a corresponding charge to other expense. After a tax credit of $445,000, the charge against earnings before extraordinary items and net earnings was $1,036,000 or 8 cents per share (6 cents fully diluted).

As of December 31, 1974, these securities were carried at cost as noncurrent assets. Market value as of December 31, 1974 was $924,000.

NONCURRENT ASSETS

MICKELBERRY CORPORATION

Consolidated Balance Sheet

• • • •

	December 27, 1975	December 28, 1974
Stockholders' Equity (Notes 6 and 7):		
Common stock, par value $1 per share		
Authorized—1,000,000 shares		
Issued—832,760 (1974—356,620)	832	356
Capital in excess of par value	244	636
Retained earnings	6,122	5,381
	7,199	6,374
Less:		
Unrealized loss on investment in marketable securities (Note 3)	188	—
Common shares in treasury, at cost (26,196 in 1974)	—	458
Total Stockholders' Equity	7,010	5,916

Consolidated Statement of Stockholders' Equity

Years Ended December 27, 1975 and December 28, 1974

	Common Stock Par Value $1	Capital In Excess of Par Value	Retained Earnings	Unrealized Loss on Investment In Marketable Securities	Common Shares In Treasury At Cost	Total Stockholders' Equity
Balance December 29, 1973	$339	$573	$4,355	$ —	$(458)	$4,810
Net income for year	—	—	1,145	—	—	1,145
Cash dividends	—	—	(39)	—	—	(39)
5% stock dividend (Note 6)	16	62	(79)	—	—	—
Balance December 28, 1974	356	636	5,381	—	(458)	5,916
Net income for year	—	—	1,353	—	—	1,353
Cash dividends	—	—	(89)	—	—	(89)
Stock splits effected in the form of stock dividends (Note 6):						
2 for 1	356	—	(356)	—	—	—
5 for 4	166	—	(166)	—	—	—
Retirement of common shares in treasury	(52)	(405)	—	—	458	—
Stock options exercised (Note 7)	5	13	—	—	—	19
Adjustment to reflect market value of investment (Note 3)	—	—	—	(188)	—	(188)
Balance December 27, 1975	$832	$244	$6,122	$(188)	$ —	$7,010

Notes to Financial Statements

3. Investment in Marketable Securities

At December 27, 1975 and December 28, 1974 the Company owned 32,100 shares of common stock of The Horn & Hardart Company (approximately 4.6% of the outstanding common stock). These shares were purchased for investment purposes and the Company has no plans to dispose of them.

The original cost of the investment was $613,100 (approximately $19 per share). Management concluded that there had been a permanent impairment in the value of the investment and, in 1973, it was written down by $292,100 (approximately $9 per share) resulting in an aggregate adjusted cost of $321,000.

In accordance with the provisions of Statement of Financial Accounting Standards No. 12 (Accounting for Certain Marketable Securities), at December 27, 1975 the investment is carried at the lower of cost or market at the balance sheet date.

At December 28, 1974 the investment was not required to be carried at the lower of cost or market at the balance sheet date and was carried at cost. Market value at December 28, 1974 was $100,300.

To reduce the carrying amount of the investment from an adjusted cost of $10 per share to market of $4 at December 27, 1975, a valuation allowance in the amount of $188,600 was established by a charge to stockholders' equity representing the unrealized loss. Based upon analysis of the underlying values of Horn & Hardart's assets and its future earnings prospects, management does not believe that the investment has been further permanently impaired.

Horn & Hardart common shares traded on the American Stock Exchange in the range of $8 to $3 during 1975 and were $4 on December 27, 1975 (in 1974, trading was in the range of $10 to $3 and was $3 on December 28, 1974). The closing market value on February 13, 1976 was $184,000 ($6 per share).

COLONIAL STORES INCORPORATED

Consolidated Balance Sheets

	January 3, 1976	December 28, 1974
••••		
Stockholders' equity (notes 2, 3, and 5):		
4% cumulative preferred stock of $50 par value per share, redeemable 1,200 shares per annum at par plus accrued dividends.		
Authorized and issued 21,102 shares (1974, 21,134 shares)	1,055	1,057
Common stock of $2.50 par value per share.		
Authorized 8,000,000 shares; issued 4,387,899 shares (1974, 4,376,424 shares)	10,970	10,941
Capital in excess of par value of capital stock	1,487	1,355
Unrealized loss on market decline of investments in preferred stocks	(588)	—
Retained earnings	92,207	83,656
	105,131	97,009
Less common stock held in treasury, 576,545 shares (1974, 559,469 shares), at cost	11,103	10,733
Total stockholders' equity	94,028	86,276

Notes to Financial Statements

(2) Investments in Preferred Stocks

In accordance with Statement No. 12 of the Financial Accounting Standards Board adopted in December 1975, the Company established a valuation allowance to reduce to market value the amount at which it carried its investment in preferred stocks, all of which exceeded market, at January 3, 1976. The allowance, in the amount of $840,000, was established by a charge to stockholders' equity of $588,000 which is net of the income tax effect of $252,000. At December 28, 1974, these investments were stated at cost and had a market value of $2,854,000.

AMERICAN TELECOMMUNICATIONS CORPORATION

Consolidated Balance Sheet

	April 30, 1976	April 30, 1975
• • • •		
Stockholders' equity		
Common stock, par value $.10 per share; authorized 4,000,000 shares; issued 1,785,657 shares and 1,773,182 shares (Note 10)	178	177
Additional paid-in capital	4,790	4,749
Retained earnings	5,106	3,789
	10,076	8,717
Less		
Unrealized loss on noncurrent marketable equity securities (Note 4)	38	
Employee benefit plan (Note 8)	600	600
Total stockholders' equity	9,437	8,117

Consolidated Statement of Stockholders' Equity

Years Ended April 30, 1976 and 1975

	Common stock	Additional paid-in capital	Retained earnings	Employee benefit plan	Unrealized loss on non-current marketable equity securities
Balance, April 30, 1974	$177	$4,731	$2,868	$	$
Net income			921		
Tax benefit arising from disqualifying dispositions of shares issued under stock options		10			
Other		7			
Reclassification of employee benefit plan (Note 8)	—	—	—	(600)	—
Balance, April 30, 1975, as reclassified	177	4,749	3,789	(600)	
Net income			1,316		
Tax benefit arising from disqualifying dispositions of shares issued under stock options		11			
Unrealized loss on non-current marketable equity securities (Note 4)					(38)
Issuance of shares upon exercise of employee stock options	1	33			
Other		(3)			
Balance, April 30, 1976	$178	$4,790	$5,106	$(600)	$(38)

Notes to Financial Statements

4. Investment in Securities

• • • •

The Company additionally holds marketable equity securities which it intends to hold for investment purposes and has therefore classified such as non-current. In accordance with Financial Accounting Standards Board Statement No. 12, "Accounting for Certain Marketable Securities," the Company has reduced the carrying amount of the non-current marketable equity securities to market, which was lower than cost at April 30, 1976. At April 30, 1976, the cost and market value of the non-current marketable equity securities were $500,000 and $461,250, respectively, and accordingly a valuation allowance in the amount of $38,750 was established by a charge to stockholders' equity representing the unrealized loss. At April 30, 1975, the cost and market value of the non-current marketable equity securities were $500,000 and $425,000, respectively.

NATIONAL GYPSUM COMPANY
Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
• • • •		
Stockholders' Equity		
$4.50 Cumulative Preferred Stock	—	10,000
Common Stock	8,551	8,550
Capital surplus	166,257	164,972
Retained earnings	170,385	165,286
	345,193	348,808
Less:		
Unrealized loss on marketable equity security	8,132	—
Cost of treasury stock	13,883	17,394
Total Stockholders' Equity	323,178	331,414

Notes to Financial Statements

Investment in H.H. Robertson Company—The company's marketable equity security represents 699,900 shares (25.8%) of the common stock of H.H. Robertson Company acquired at a cost of $22,746,000, or $32.50 per share. H.H. Robertson Company stock is listed on the New York Stock Exchange. The following summary is based on their published financial information:

	1975 Thousands	1974 Thousands
H.H. Robertson Company:		
Net sales	$343,972	$338,573
Net income	$ 16,405(a)	$ 7,282
Less dividends	3,662(est.)	3,532
Undistributed net income	12,743(est.)	3,750
25.8% thereof	3,288	968
Shareholders' equity	$ 87,979(est.)	$ 75,236
25.8% thereof	22,699	19,411

(a) Includes gain of $3,600,000 from change in accounting for translation of foreign currency.

	1975	1974
National Gypsum's investment at cost	$ 22,746	$ 22,746
Market quotation:		
End of year	14,614	9,099
February 17, 1976	17,760	—

The company in compliance with Financial Accounting Standards Board Statement No. 12, reduced the carrying amount of these shares to the quoted market value at December 31, 1975, by establishing a valuation allowance in the amount of $8,132,000 which was charged to stockholders' equity. The equity method is not applicable because of the terms of a Consent Judgment entered into on July 17, 1973 as a result of a law suit brought by Robertson in 1970. The Consent Judgment does not limit or restrict the ability of the company to use, dispose of or add to its holdings of Robertson common stock. However, if the company decides to purchase or acquire any additional shares of Robertson common stock by tender offer or otherwise, to attempt to elect its nominee as a member of the Robertson Board of Directors, or to attempt to call a special meeting of the Robertson stockholders, it is obliged to give Robertson and the Federal Courts written notice thereof in reasonable detail not less than five business days prior to undertaking such action. In such event, Robertson may apply to the Courts for any relief it deems appropriate.

SANTA FE INDUSTRIES, INC.
Statement of Stockholders' Equity for the Year

	1975	1974
Capital Stock (Note 8)		
Balance at beginning of year	$ 272,499	$ 271,234
Conversion of 6¼% Subordinated Debentures	2	3
Conversion of $.50 Cumulative Preferred Stock	(202)	(242)
Exercise of stock options (Note 9)	136	1,504
Balance at end of year	272,435	272,499
Paid-in Capital		
Balance at beginning of year	23,990	20,744
Conversion of 6¼% Subordinated Debentures	4	7
Conversion of $.50 Cumulative Preferred Stock	202	242
Exercise of stock options (Note 9)	210	2,801
Federal income tax benefits from employes' dispositions of stock option shares (Note 9)	7	196
Balance at end of year	24,413	23,990
Retained Income		
Balance at beginning of year	1,193,485	1,120,329
Net income	109,194	120,051
Dividends declared		
Preferred stock—$.50 per share	(805)	(814)
Common stock—$1.80 per share	(46,100)	(46,081)
Balance at end of year	1,255,774	1,193,485
Valuation Allowance for Marketable Equity Securities (Note 10)	(1,392)	—
Treasury Stock		
25,835 shares of common stock, at cost	(811)	(811)
Total	$1,550,419	$1,489,163

Notes to Financial Statements

Note 10: Valuation Allowance for Marketable Equity Securities

In accordance with Statement No. 12 issued by the Financial Accounting Standards Board, a valuation allowance of $1,989,000 was recorded by a charge to stockholders' equity in 1975 to reduce the cost of marketable equity securities ($7,588,000 included in Voluntary Bond Retirement Fund and $9,205,000 included in other assets) to market value at December 31, 1975. The amount charged to stockholders' equity has been reduced by $597,000 representing the tax benefits that would be realized by Santa Fe in the event such loss was incurred upon disposition of the securities.

CHESSIE SYSTEM, INC.
Consolidated Balance Sheets

	December 31, 1975	December 31, 1974
• • • •		
Shareowners' Equity		
Common stock, par value $12.50 per share	236,496	230,077
Other capital	436,319	428,123
Earnings reinvested in the business	403,972	351,551
	1,076,787	1,009,751
Less		
Unrealized loss on marketable equity securities (note 1)	3,200	—
Treasury stock at cost (138,373 shares in 1975 and 116,068 shares in 1974)	3,571	2,828
	6,771	2,828
Total shareowners' equity	1,070,016	1,006,923

Consolidated Statements of Changes in Shareowners' Equity

Years Ended December 31, 1975 and 1974

(Thousands of Dollars)

	Shares Outstanding	Common Stock	Other Capital	Earnings Reinvested in the Business	Unrealized Loss on Marketable Equity Securities	Treasury Stock
Balance at December 31, 1973	17,242,284	$218,903	$413,714	$289,755	$ —	$6,226
Earnings for the year	—	—	—	95,249	—	—
Exchange of common stock for B&O Series G bonds	893,930	11,174	14,415	—	—	—
Dividends on common stock, $1.875 per share	—	—	—	(33,453)	—	—
Purchase of treasury stock	(144,542)	—	—	—	—	3,458
Issued for B&O stock	209,026	—	—	—	—	(4,823)
Issued for Aviation Enterprises, Inc. stock	81,846	—	—	—	—	(1,859)
Issued under Management Incentive Plan	7,544	—	—	—	—	(174)
Other changes	(4)	—	(6)	—	—	—
Balance at December 31, 1974	18,290,084	230,077	428,123	351,551	—	2,828
Earnings for the year	—	—	—	91,412	—	—
Exchange of common stock for B&O Series G bonds	327,407	4,093	5,279	—	—	—
Common stock sold to employees (note 8)	186,104	2,326	2,917	—	—	—
Dividends on common stock, $2.10 per share	—	—	—	(38,991)	—	—
Purchase of treasury stock	(22,305)	—	—	—	—	743
Reduction in carrying value of marketable equity securities	—	—	—	—	3,200	—
Balance at December 31, 1975	18,781,290	$236,496	$436,319	$403,972	$3,200	$3,571

Notes to Financial Statements

(1) Significant Accounting Policies

• • • •

As required by a statement of the Financial Accounting Standards Board issued in December, 1975, marketable equity securities included in noncurrent investments are carried at market value at December 31, 1975. Such investments were carried at cost at December 31, 1974. The aggregate cost of marketable equity securities amounted to $10.4 million at December 31, 1975 and 1974. To reduce the carrying value of these securities to market value of $7.2 million at December 31, 1975, a valuation allowance of $3.2 million was established by a charge to shareowners' equity. The potential tax benefit of the unrealized capital loss has not been recognized. There are no marketable equity securities owned at December 31, 1975 with market values in excess of cost. • • • •

FILMWAYS, INC.
Consolidated Balance Sheets

	February 29, 1976	February 28, 1975
• • • •		
Shareholders' Equity:		
Preferred stock, par value $1—authorized 200,000 shares (liquidation preference $4,911,400); outstanding (Note 7):		
Series A—16,614 shares	246	246
Series B—32,500 shares	333	333
Common stock par value $.25—authorized 5,000,000 shares; issued 2,058,329 and 1,866,524 shares (Notes 8 and 12):	515	467
Paid-in surplus (Note 12)	13,150	11,647
Retained earnings (Notes 6 and 12)	2,899	2,386
Unrealized loss on noncurrent marketable equity securities (Note 4)	(163)	—
Treasury stock, at cost (74,622 shares)	(343)	(343)
Total shareholders' equity	16,637	14,736

Notes to Financial Statements

(4) Investments

Investments include land, as well as common stock in a nonaffiliated company. The original cost of the stock was $706,000 and its market value at February 29, 1976 was $343,000. In previous years, the Company established a valuation reserve to reflect the permanent decline in aggregate net realizable value which the Company's investments have suffered. In compliance with Statement of Financial Accounting Standards No. 12, the Company has further reduced the carrying value of the stock to market value, at February 29, 1976, reflecting said write-down of $163,000 as a reduction of shareholders' equity.

LFE CORPORATION
Consolidated Balance Sheet

	April 30 1976	April 25 1975
• • • •		
Stockholders' Investment (Note 9)		
Series preferred stock		
Authorized 500,000 shares		
Outstanding 165,839 shares in 1976 and 1975, Series A, Cumulative, Convertible (two shares preferred stock into one share of common stock), stated value $10 per share, $.50 annual dividend (entitled in liquidation to $14 per share or $2,322,000)	$ 1,658	$ 1,658
Common stock, par value $1 per share		
Authorized 4,000,000 shares		
Outstanding 1,973,228 shares in 1976 and 1,973,236 shares in 1975	1,973	1,973
Premium on common stock	17,166	17,166
Net unrealized loss on noncurrent marketable securities (Note 3)	(349)	—
Retained earnings (deficit)	(471)	(914)
Total stockholders' investment	$19,977	$19,883

Notes to Financial Statements

3. Investments

At April 30, 1976, marketable equity securities are carried at the lower of cost or market pursuant to the requirements of Statement No. 12 of the Financial Accounting Standards Board. The cost of these securities which represents common stock of Epsco, Incorporated was $477,000. To reduce the carrying amount of these securities to market, a valuation allowance in the amount of $349,000 was established by a charge to stockholders' equity representing the unrealized loss.

At April 25, 1975, these marketable securities were not required to be carried at the lower of cost or market and were carried at cost. The market value was $140,000 on April 25, 1975.

MILTON ROY COMPANY
Consolidated Balance Sheet

	As of December 31, 1975	1974
••••		
Shareholders' equity:		
Common stock, $1 par value, authorized 2,000,000 shares, issued 1,363,920 and 1,305,469 shares	1,363	1,305
Paid-in capital	5,620	5,310
Retained earnings	16,674	15,042
	23,658	21,658
Less: 6,950 and 24,751 shares of common stock in treasury, at cost	27	154
Unrealized loss on marketable securities	119	—
Total shareholders' equity	23,512	21,504

Consolidated Statement of Shareholders' Equity

	Common stock $1 par value	Paid-in capital	Retained earnings	Treasury stock Shares	Treasury stock Amount	Unrealized loss on marketable securities	Shareholders' equity
Balance December 31, 1973	$1,305	$5,477	$13,382	(14)	$ (54)	$ —	$20,110
Net income	—	—	1,917	—	—	—	1,917
Sale of treasury stock to employees pursuant to employee stock purchase plan	—	(166)	—	17	332	—	166
Common shares received upon divestiture of division	—	—	—	(14)	(247)	—	(247)
Unearned escrow shares returned	—	—	—	(2)	(84)	—	(84)
Purchase of treasury stock	—	—	—	(10)	(100)	—	(100)
Dividends—20¢ per share	—	—	(257)	—	—	—	(257)
Balance December 31, 1974	1,305	5,310	15,042	(24)	(154)	—	21,504
Net income	—	—	1,889	—	—	—	1,889
Sale of treasury stock and issuance of new shares to employees pursuant to employee stock purchase plan	7	99	—	11	70	—	177
Sale of treasury stock to the Company's retirement profit sharing plan	—	5	—	5	56	—	61
Employee stock option exercised	1	5	—	—	—	—	6
Common shares issued for an acquisition	50	200	—	—	—	—	250
Unrealized loss on marketable securities	—	—	—	—	—	(119)	(119)
Dividends—20¢ per share	—	—	(258)	—	—	—	(258)
Balance December 31, 1975	$1,363	$5,620	$16,674	(6)	$ (27)	$(119)	$23,512

Notes to Financial Statements

Note 3—Marketable equity securities:

Certain noncurrent marketable equity securities are included in other assets. Effective December 31, 1975 such securities are required by a recent pronouncement of the Financial Accounting Standards Board to be carried at the lower of cost or market. To reduce the carrying amount of these securities to market, ($203,175) which was lower than cost ($322,470) at December 31, 1975, a valuation allowance in the amount of $119,295 was established by a charge to shareholders' equity representing the unrealized loss. At December 31, 1974, such securities were not required to be carried at the lower of cost or market. At that date the cost of the portfolio ($270,000) exceeded the market value ($198,000) by $72,000.

OVERSEAS SHIPHOLDING GROUP, INC.

Consolidated Balance Sheets

	As at December 31, 1975	1974 as adjusted—Note A(8)
• • • •		
Stockholders' Equity—Notes E, H and K:		
Common Stock, par value $1 per share:		
Authorized—20,000,000 shares		
Issued and outstanding—9,750,430 shares	9,750	9,750
Paid-in Additional Capital	12,068	12,068
Retained Earnings	150,698	114,173
	172,517	135,992
Less: net unrealized loss on marketable equity securities	(2,128)	—
	170,388	135,992

Notes to Financial Statements

Note A—Summary of Significant Accounting Policies:

• • • •

7. As at December 31, 1975, pursuant to Statement of Financial Accounting Standards No. 12 of the Financial Accounting Standards Board, investments in marketable equity securities (including marketable equity securities included in Interim Capital Construction and Restricted Funds) are carried at the lower of aggregate cost or market and the amount of the allowance for net unrealized loss on marketable equity securities is shown as a reduction of stockholders' equity. Investments in marketable securities, other than equity securities, are carried at cost. As at December 31, 1974, investments in marketable securities were all carried at cost. Management intends to hold the securities (which are substantially income producing) included in Investments in Marketable Securities as long-term investments and believes that the Company will not require the use of these funds during 1976. Management also believes that the cost of the marketable securities will ultimately be recovered (see Note E).

CURRENT AND NONCURRENT ASSETS

FRESNILLO COMPANY

Consolidated Balance Sheets

	At December 31 1975	1974
• • • •		
Shareholders' Equity (Note 5):		
Common stock, $1 par value:		
Authorized 2,100,000 shares, Issued 1,152,081 shares, 1975; 1,100,018 shares, 1974	1,152	1,100
Capital surplus	3,031	1,417
Retained earnings (Note 4)	21,908	21,373
Treasury stock, 27,238 shares, at cost	(304)	(304)
Shareholders' equity before valuation allowance	25,786	23,586
Net unrealized loss on noncurrent marketable equity securities (Note 2)	(3,421)	—
Total shareholders' equity	22,365	23,586

Consolidated Statements of Income and Retained Earnings

	for years ended December 31	
	1975	1974
••••		
Costs and Expenses:		
General and administrative	289	254
Exploration	147	116
Net unrealized loss on current marketable equity securities (Note 2)	194	—
Write down of investments (Note 2)	—	1,836
	632	2,207

Notes to Financial Statements

2. In accordance with Statement No. 12 of the Financial Accounting Standards Board, the current and non-current portfolios of marketable equity securities at December 31, 1975 are each carried at the lower of cost or market. This accounting method was not required at December 31, 1974, and accordingly, the current portfolio was carried at cost and the non-current at cost or less. At December 31, 1975, marketable equity securities (included in current assets) had a cost of $1,831,545 and noncurrent marketable equity securities (not included in current assets) had an adjusted cost basis of $5,755,964.

To reduce the carrying amount of the current marketable equity securities portfolio to market at December 31, 1975, which was then lower than cost, a valuation allowance of $194,519 representing the net unrealized loss was established with a corresponding charge to income. To reduce the carrying amount of the noncurrent marketable equity securities portfolio to market at December 31, 1975, which was then lower than adjusted cost, a valuation allowance of $3,421,269 was established by a charge to shareholders' equity representing the net unrealized loss. The valuation allowance for the noncurrent portfolio is primarily attributable to the decline in the market value of the Company's investment in Kawecki Berylco Industries, Inc. (324,635 common shares). As of March 12, 1976, the market values of the above-mentioned current and noncurrent marketable equity security portfolios have increased by $219,000 and $821,000, respectively.

At December 31, 1975, gross unrealized gains and (losses) of current and noncurrent marketable equity securities were as follows: current, $36,293 and ($230,812); noncurrent, $62,249 and ($3,483,518).

In 1974, in light of the continuing period of market decline of the Company's investment in Kawecki, management considered it conservative to adjust its cost ($7,079,000) to the underlying book value of Kawecki at December 31, 1974, resulting in a charge to income of $1,323,300. In addition, another investment with a cost of $513,200 was written down in 1974 to a nominal value. At December 31, 1974, current and noncurrent marketable equity securities had market values of $1,115,000 and $3,491,000, respectively.

In computing realized gains or losses on the sale of securities, cost is determined on the first-in, first-out method.

HOMESTAKE MINING COMPANY
Consolidated Balance Sheet

	December 31	
	1975	1974
••••		
Shareholder Equity:		
Capital stock, $1 par value:		
Preferred: 4,000,000 shares authorized; no shares outstanding		
Common: 36,000,000 shares authorized; 11,332,268 shares outstanding	11,332	11,300
Capital surplus	48,471	47,763
Earned surplus	73,677	63,601
Unrealized loss on marketable mining securities	(3,227)	—
Total	130,253	122,664

Statement of Consolidated Income

	for the Years Ended December 31	
	1975	1974
Revenues:		
Sales:		
Gold	$65,670	$59,803
Lead and zinc	31,749	51,146
Uranium	10,521	1,685
Silver	6,394	6,349
Forest products	2,005	2,838
Interest and dividends	4,215	4,591
Marketable equity security losses	(454)	(2,669)

● ● ● ●

Notes to Financial Statements

Summary of Significant Accounting Policies

● ● ● ●

Marketable securities are segregated into three basic portfolios: U.S. government obligations and commercial notes, utility and industrial preferred stocks, and equity mining securities. The first two portfolios are classified as current assets and the other portfolio as a noncurrent asset. Realized gains and losses are included in the determination of income of the period in which they occur; cost of securities sold is determined by the specific identification method.

U.S. government obligations and commercial notes are carried at cost which approximates market valuation. Current and noncurrent portfolios of marketable equity securities are each carried at their lower of cost or market valuation at balance sheet dates; net unrealized losses in the current portfolio are included in the determination of income and such losses in the noncurrent portfolio are reported as a reduction of shareholder equity. See following note for information with respect to changes in accounting methods and other related matters.

● ● ● ●

Marketable Equity Securities

Information with respect to marketable equity securities follows:

	Preferred Stocks	Mining Securities
At December 31, 1975:		
Aggregate cost	$ 9,113,000	$7,310,000
Unrealized (losses):		
Included in income:		
1974	(1,500,000)	
1975	182,000	
Direct reduction of shareholder equity		(3,227,000)
Carrying amounts (aggregate market valuation)	$ 7,795,000	$4,083,000
At December 31, 1974:		
Aggregate cost	$13,536,000	$6,468,000
Allowance for decline in market valuation based upon information available in February 1975	1,500,000	
Carrying amounts	$12,036,000	$6,468,000
Aggregate market valuation	$11,006,000	$5,804,000

Net realized losses of $636,000 in 1975 and $1,169,000 in 1974 on the sale of marketable equity securities have been included in income. Income tax benefits applicable to security losses have been recognized to the extent of offsetting realized capital gains.

Effective as of December 31, 1975, Homestake, in order to conform with a standard of financial accounting and reporting issued by the Financial Accounting Standards Board in December 1975, adopted the methods of accounting for marketable equity securities described in the preceding note to financial statements. Previously, preferred stocks, classified as a current asset, were carried at cost less allowances made in recognition of significant market valuation declines not reasonably certain to be temporary; mining securities, classified as a noncurrent asset, were carried at cost and impairments in market valuations which were considered to be permanent were provided for at the time such condition became evident. Had the new methods been in effect in prior years, reported net income of $24,230,000 ($2.14 per share) would have been increased by $1,029,000 ($.09 per share) in 1975 and reported net income of $34,100,000 ($3.01 per share) would have been decreased by $281,000 ($.02 per share) in 1974.

E.F. MAC DONALD COMPANY

Consolidated Balance Sheet

	February 1 1976	February 2 1975
••••		
Stockholders' Equity		
Contributed capital (Note J)		
Common stock	1,257	1,257
Additional contributed capital	5,578	5,578
Retained earnings (deficit)	2,704	(714)
	9,540	6,121
Less		
Common stock held in treasury—at cost (Note J)	56	56
Net unrealized loss in noncurrent marketable equity securities (Note B)	4,175	—
	5,308	6,064

Consolidated Statement of Earnings

	Years ended February 1 1976	Years ended February 2 1975
••••		
Operating profit	6,184	2,529
Other income (expense)		
Interest and dividend income	1,256	1,366
Rental income—net	387	347
Realized gain on sale of securities	23	91
Unrealized gain (loss) in market value of current equity securities	89	(136)
••••		

Notes to Financial Statements

Note B—Marketable Equity Securities

At February 1, 1976, the current and noncurrent portfolios of marketable equity securities were each carried at their lower of cost or market at the balance sheet date. Marketable equity securities included in current and noncurrent assets had a cost of $712,920 and $16,740,697, respectively, at February 1, 1976. To reduce the carrying amount of the noncurrent marketable equity securities portfolio to market, which was lower than cost at February 1, 1976, a valuation allowance in the amount of $4,175,387 was established by a charge to stockholders' equity representing the net unrealized loss.

At February 2, 1975, the noncurrent portfolio of marketable equity securities was not required to be carried at the lower of cost or market and was carried at a cost of $17,134,459 although the market value was $11,116,294. The current portfolio was carried at the lower of cost ($1,280,857) or market ($1,144,092).

••••

UNCLASSIFIED BALANCE SHEET

FINANCIAL SERVICES COMPANIES
Combined Balance Sheet

	December 31 1975	1974
	(millions of dollars)	
••••		
Shareholder's equity:		
Capital stock	22.0	21.1
Paid-in capital from Borg-Warner Corporation	29.0	29.9
Unrealized loss on marketable securities	(1.0)	—
Retained earnings	44.7	37.7
Total shareholder's equity	94.7	88.7

Notes to Financial Statements

Accounting Changes

At December 31, 1975 marketable securities had a carrying value of $14.1 million and a cost of $15.1 million. The cost of certain marketable equity securities at December 31, 1975 was reduced to market value by establishment of a valuation allowance of $1.0 million with a corresponding charge to shareholder's equity. At December 31, 1974, marketable securities were not required to be carried at the lower of cost or market, and were carried at a cost of $5.4 million (market value $4.2 million).

••••

NATIONAL KINNEY CORP.
Consolidated Balance Sheet

	December 31 1975	1974
••••		
Shareholders' equity (Notes 11 and 12):		
Convertible Preferred shares, par value $1 per share, 1,500,000 shares authorized	1,500	1,500
Common shares, par value $1 per share, 15,000,000 shares authorized	6,432	6,432
Paid in capital	49,791	49,791
Retained earnings (deficit)	(8,882)	8,395
Net unrealized loss on marketable equity securities	(4,149)	—
Less 85,000 Common shares held in treasury at cost	(368)	(368)
Total shareholders's equity	44,324	65,750

Summary of Significant Account Policies

••••

Marketable equity securities

At December 31, 1975 the portfolio of marketable equity securities is carried at the aggregate quoted market value which is lower than its cost of $15,493,000 in accordance with Statement of Financial Accounting Standards No. 12 "Accounting for Certain Marketable Securities."

To reduce the portfolio to its aggregate market value, a valuation allowance of $4,149,000 representing the aggregate unrealized loss was established by a charge to shareholders' equity. (At March 31, 1976, the unrealized loss has been reduced to $3,572,000.) A realized loss of $300,000 was charged to operations in 1975 as the result of the write-down of marketable equity securities.

At December 31, 1974, the portfolio of marketable equity securities was not required to be carried at the lower of cost or market at the balance sheet date and was carried at cost.

In the opinion of management, the decline in the market value of the portfolio is not of a permanent nature.

••••

UNICAPITAL CORPORATION
Consolidated Statement of Stockholders' Investment

For the years ended February 29, 1976 and February 28, 1975

	$1 Par Common Stock	Paid-In Surplus	Retained Earnings	Valuation Reserve for Marketable Securities	Treasury Stock
Balance, February 23, 1974 5,411,214 shares (311,500 in treasury)	$5,411	$20,015	$18,132	$ —	$(2,688)
Net income			316		
Purchase of 234,000 treasury shares					(1,239)
Cash dividends of $.12 per share			(593)		
Balance, February 28, 1975 5,411,214 shares (545,500 in treasury)	5,411	20,015	17,855	—	(3,927)
Net income			1,378		
Purchase of 260,000 treasury shares					(533)
Valuation reserve for marketable securities (Note 1)				(1,151)	
Balance, February 29, 1976 5,411,214 shares (805,500 in treasury)	$5,411	$20,015	$19,233	$(1,151)	$(4,460)

Notes to Financial Statements

1. Statement of Significant Accounting Policies

• • • •

Marketable securities are also included in other assets and, in conformity with the Financial Accounting Standards Board's statement entitled "Accounting for Certain Marketable Securities," the Company's investment in marketable securities has been stated at the lower of cost or market as of February 29, 1976. To reduce the carrying amount of these investments to market ($845,000), which was lower than cost ($1,996,000), a valuation allowance in the amount of $1,151,000 was established by a charge to Stockholders' Investment.

Realized marketable security losses of $121,000 in 1976 and $1,257,000 in 1975 were charged against earnings as incurred.

ASSIGNMENT OF A NEW COST BASIS

For those marketable securities for which the effect of a change in carrying amount is included in stockholders' equity rather than in net income (including marketable securities in unclassified balance sheets), Statement No. 12 requires a determination to be made as to whether a decline in market value below cost as of the balance sheet date of an individual security is other than temporary. If the decline is judged to be other than temporary, the cost basis of the individual security is required to be written down to a new cost basis and the amount of the write down is to be accounted for as a realized loss. The new cost basis is not to be changed for subsequent recoveries in market value.

One example of the assignment of a new cost basis to individual marketable equity securities classified as noncurrent assets is presented.

THE RALPH M. PARSONS COMPANY

Consolidated Balance Sheet

	December 26, 1975	December 27, 1974
••••		
Total current assets	143,935	102,011
Marketable securities, at cost, less allowance for decline in market value		6,010
••••		

Consolidated Statement of Income

	Fiscal year ended December 26, 1975	Fiscal year ended December 27, 1974
Income:		
Revenues from engineering and construction contracts	$832,420	$391,236
Interest and dividends, less provision for decline in market value of marketable securities	2,526	3,802
	834,946	395,038
••••		

Notes to Financial Statements

Note C—Marketable securities:

In 1973, the Company invested $6,710,000 in certain preferred stocks, the quoted market value of which vacillated significantly subsequent to their purchase. In 1974, Management did not expect to sell these securities during 1975 and made allowance for $700,000, before anticipated income tax benefits, to reduce their carrying value for the estimated permanent impairment and reclassified the securities from current to non-current investments. Because of income tax considerations, Management decided in mid-1975 to sell these securities; the substantial portion was sold prior to yearend at an additional loss, before anticipated income tax benefits, of $800,000 (including provision for loss on the remainder which was sold in January 1976). The amounts provided for the declines in market value of these securities have been charged against income from interest and dividends.

IV

INVESTEES ACCOUNTED FOR BY THE EQUITY METHOD

ESTABLISHMENT OF VALUATION ALLOWANCES

Investors, in preparing consolidated financial statements, must determine how to handle investments of the investee in conformity with FASB Statement No. 12. Although the Statement does not discuss the reporting that should be made in the consolidated financial statements of the investor to the establishment of a valuation allowance with a corresponding charge to stockholders' equity by an investee, an acceptable method consists of writing down the investment in the investee to reflect the reduction in its net assets. The amount of the writedown is reported as a separate item of consolidated stockholders' equity.

Six examples are presented of companies that wrote down the investment in investees and reported the amount of the writedown as a separate item of consolidated stockholders' equity.

ALLEGHANY CORPORATION
Consolidated Balance Sheets

	December 31, 1975	1974
••••		
Stockholders' equity (notes 4 and 6)		
Capital stock:		
Common, par value $1; authorized 22,000,000 shares; 510,490 shares reserved for warrants and options (514,190 in 1974); issued 8,507,250 shares (8,503,550 in 1974), less 673,940 shares held in treasury	7,833	7,829
Additional paid-in capital	114,407	114,397
	122,240	122,226
Net unrealized depreciation of marketable equity securities of Investors Diversified Services, Inc. (note 3)	(3,843)	—
Retained earnings	49,076	46,913
Total stockholders' equity	167,474	169,140

Notes to Financial Statements

(3) Equity Method of Accounting:

The Corporation has the ability to exercise significant influence with respect to IDS by reason of its ownership of approximately 45% of the voting stock and 29% of the equity of IDS, and therefore accounts for its holdings of IDS by the equity method.

••••

In December, 1975 the Financial Accounting Standards Board ("FASB") issued *Statement of Financial Accounting Standards No. 12*, "Accounting for Certain Marketable Securities", which is effective for years ending on or after December 31, 1975 and which requires certain marketable equity securities (exclusive of investments accounted for by the equity method) to be carried at the lower of cost or market. As required by the Statement, IDS, which had previously carried such investments at average cost, reduced the carrying value of certain marketable equity securities to the lower of cost or market through a charge against net worth as of December 31, 1975. The Corporation has recognized as of such date its share ($5,538,000) of such charge through a reduction in the carrying value of its investment in IDS and a corresponding charge against net worth, net of deferred tax benefits.

● ● ● ●

ARMCO STEEL CORPORATION
Statement of Consolidated Financial Position

	December 31, 1975	December 31, 1974
● ● ● ●		
Shareholders' Equity (Note 2)		
Preferred stock—authorized 4,333,100 shares of no par value, issuable in series. Series issued: $2.10 cumulative convertible (involuntary liquidation preference aggregates approximately $51,000)	14,459	14,460
Common stock—authorized 60,000,000 shares of $5 par value each	147,011	146,363
Additional paid-in capital	118,266	116,184
Income retained in the business	1,055,291	992,758
Net unrealized losses on marketable equity securities of unconsolidated subsidiaries (Note 9)	(4,284)	—
Total Shareholders' Equity	1,330,743	1,269,765

Statement of Consolidated Shareholders' Equity

For the years ended December 31, 1975 and 1974

	Preferred Stock Shares	Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Income Retained in the Business	Net Unrealized Losses (Note 9)
Balance, January 1, 1974 as previously reported (after deducting 528,562 common shares in treasury)	3,722,595	$15,821	29,263,925	$146,320	$115,529	$ 867,584	—
Restatement for accounting changes (Notes 1&7)						(4,266)	
Balance, January 1, 1974 as restated						863,318	
Treasury stock issued in connection with acquired businesses—net			8,728	43	627		
Exercise of stock options	1,313	6			28		
Purchase of preferred stock, for retirement	(321,600)	(1,367)				(8,245)	
Net income as previously reported						204,260	
Effect of accounting changes						(651)	
Cash dividends							
Common						(58,660)	
Preferred						(7,264)	
Balance, December 31, 1974 (after deducting 519,834 common shares in treasury)	3,402,308	14,460	29,272,653	146,363	116,184	992,758	—

Treasury stock issued in connection with acquired businesses—net			19,996	100	337		
Exercise of stock options			109,475	547	1,745		
Exchange of preferred shares	(208)	(1)	176	1			
Net income						116,661	
Cash dividends							
Common						(46,984)	
Preferred						(7,144)	
Adjustment for net unrealized losses on marketable equity securities of unconsolidated subsidiaries..........							(4,284)
Balance, December 31, 1975 (after deducting 390,187 common shares in treasury)	3,402,100	$14,459	29,402,300	$147,011	$118,266	$1,055,291	($4,284)

Notes to Financial Statements

9. Bellefonte Insurance Companies

• • • •

Summary of Significant Accounting Policies
Insurance Accounting

• • • •

In 1975, the companies in accordance with accounting practices allowed in the property and liability insurance industry elected to carry their marketable equity securities (stocks) at market value. The difference between cost and market value, $6,120,000, less deferred taxes, $1,836,000, is recorded as a reduction in parent's equity on Bellefonte's statement of consolidated financial position. The net amount, $4,284,000, is also recorded on Armco's statement of consolidated financial position as net unrealized losses on marketable equity securities of unconsolidated subsidiaries.

• • • •

INTERNATIONAL MINING CORPORATION
Consolidated Balance Sheet

	December 31	
	1975	1974
• • • •		
Shareholders' Equity:		
Common stock issued—3,227,437 shares..................................	5,379	5,379
Capital in excess of par value of stock.....................................	3,915	3,915
Retained earnings..	53,065	50,088
Treasury stock, 721,705 shares at cost	(7,589)	(7,589)
Shareholders' equity before valuation allowance.......................	54,770	51,793
Net unrealized loss on noncurrent marketable securities (including $2,725,664 for affiliates and majority-owned subsidiary)............	(4,661)	—
Shareholders' equity applicable to 2,505,732 shares	50,108	51,793

Notes to Financial Statements

Note 1:
Summary of Accounting Policies

• • • •

Marketable Securities and Miscellaneous Investments

Noncurrent marketable equity securities are carried at the lower of aggregate average cost or aggregate market value at December 31, 1975. The amount by which the aggregate cost of noncurrent marketable equity securities exceeds the aggregate market value together with the Corporation's share of similar provisions recorded by its affiliates and majority-owned subsidiary is recorded as a reduction of shareholders' equity. At December 31, 1974, marketable securities were carried at cost less a reserve.

• • • •

Note 2:
Change in Accounting

In 1975, the Corporation, its majority-owned subsidiary, Pato Consolidated Gold Dredging Limited, and its affiliates adopted Financial Accounting Standard #12 "Accounting for Certain Marketable Equity Securities." The accounting standard requires that marketable equity securities be valued at the lower of aggregate cost or market. The excess, if any, of cost over market for securities classified as noncurrent assets is charged to shareholders' equity as an unrealized loss. The excess of cost over market for securities classified as current assets is charged to income. The Corporation is also required to record its interest in unrealized losses recorded by subsidiaries and affiliates which are accounted for by the equity method.

The effect of this change is to reduce the Corporation's shareholders' equity by $4,662,000, net of tax benefit, as follows:

Reduction in IM's marketable equity securities	$2,750,000
Reduction of its investment in Pato	2,989,000
Reduction of its investments in affiliates	722,000
	6,461,000
Less related tax benefit	1,799,000
	$4,662,000

INTERNATIONAL TELEPHONE AND TELEGRAPH CORPORATION

Consolidated Balance Sheets

	December 31, 1975	1974
• • • •		
Stockholders' Equity		
Cumulative preferred stock (Page 27)	576,646	578,101
Common stock—Authorized 150,000,000 shares, $1 par value Outstanding 94,324,038 and 94,393,892 shares	94,324	94,394
Capital surplus	550,203	555,129
Unrealized loss on marketable equity securities (net of tax benefit of $26,635)	(60,005)	—
Retained earnings	3,091,143	2,906,385
	4,252,311	4,134,009

Consolidated Income

	Years ended December 31, 1975	1974
• • • •		
Equity in Earnings (after tax)		
Hartford Fire Insurance Company (Page 37)	82,188	81,099
Financial subsidiaries (Page 34)	22,326	32,551
Decrease (increase) in unrealized loss on marketable equity securities of $130,651 and ($240,907) (net of taxes of $60,325 and tax benefit of $100,474 in 1975 and 1974) have not been included in reported income.		
Income from Operations	1,032,222	1,045,473

• • • •

Notes to Financial Statements

Marketable Equity Securities

In order to conform with FASB Statement No. 12 "Accounting for Certain Marketable Securities," investments in marketable equity security portfolios are carried at the lower of cost or market and valuation allowances will be provided to reduce cost to market if cost exceeds quoted market. No valuation allowance was required as of December 31, 1975 with respect to such investments ($26,242,000) of the Corporation and its consolidated subsidiaries since there was an unrealized gain of $8,404,000. In the case of insurance subsidiaries, provisions for valuation allowances are reflected in stockholders' equity.

Unrealized gains and losses in the portfolios of Hartford and other insurance subsidiaries are shown below (in thousands of dollars):

	March 10	December 31	
	1976	1975	1974
Gross unrealized gains—			
Hartford	$ 78,220	$ 70,175	$ 35,307
Others	2,399	1,791	510
Gross unrealized losses—			
Hartford	(105,136)	(143,481)	(284,940)
Others	(13,422)	(15,198)	(28,743)
Applicable tax effect—			
Hartford	7,873	22,890	79,394
Others	2,995	3,768	7,646
Minority interest	19	50	170
	$(27,052)	$(60,005)	$(190,656)

KATY INDUSTRIES, INC.

Consolidated Balance Sheet

	December 31,	
	1975	1974
••••		
Stockholders' equity: (Notes 1, 2, 3, 6, 7, 8, 9, 10 and 15)		
Class A preferred stock, $25 par value; authorized 2,000,000 shares, issuable in series—Series A, 5% cumulative convertible, authorized and issued 92,004 shares	2,300	2,300
Class B preferred stock, without par value; authorized 2,000,000 shares, issuable in series—$1.46 Series, cumulative convertible, stated value $10 per share; authorized 1,400,000 shares, issued 1,232,724 shares (1974—888,889 shares), liquidation preference of $25 per share—$30,818,100	12,327	8,889
Common stock, $1 par value; authorized 15,000,000 shares, issued 4,800,921 shares (1974—4,800,759 shares)	4,801	4,801
Capital surplus	21,269	19,438
Unrealized depreciation on marketable equity investments	(506)	—
Retained earnings	16,872	33,910
Treasury stock	(944)	(908)
Total stockholders' equity	56,119	68,430

Notes to Financial Statements

2. Investments:

Bush Universal, Inc.

••••

The changes in Katy's equity in Bush Universal, Inc. during the years 1975 and 1974 were as follows:

	1975	1974
	(Thousands of dollars)	
Balance, beginning of year	$19,824	$18,000
Equity in income (loss) for the period	(2,903)	1,823
Additional investment	4,853	1
Unrealized depreciation on marketable equity investments	(506)	—
Increase in equity due to estimated purchase price of remaining outstanding shares and treasury stock purchases	1,174	—
Balance, end of year	$22,442	$19,824

Bush decreased its stockholder's equity $1,808,000 at December 31, 1975 for the net unrealized depreciation on marketable equity investments in accordance with FASB Statement No. 12, and, therefore, Katy has recorded a decrease to its stockholders' equity of $506,000 representing the unrealized depreciation on marketable equity investments from its adjusted basis.

MOLYCORP, INC.
Consolidated Balance Sheet

	Dec. 31, 1975	Dec. 31, 1974
• • • •		
Stockholders' Equity (Note 8)		
Capital stock—$1.00 par value per share		
$2.50 cumulative convertible preferred stock		
Authorized ....500,000 shares		
Outstanding ....201,007 shares	$ 201	$ 201
(Liquidation preference $10,050,350)		
Common stock		
Authorized ....5,000,000 shares		
Outstanding ....2,892,055 shares	2,892	2,891
Capital in excess of par value	44,600	44,597
Retained earnings	45,193	39,667
Net unrealized loss on noncurrent marketable securities of an equity affiliate (Note 3)....	(1,157)	—
Total Stockholders' Equity	$91,729	$87,357

Notes to Financial Statements

3. Investments

• • • •

Company's Equity Investment in CBMM:

	1975	1974
Equity in undistributed earnings beginning of year....	$13,583,716	$ 8,326,225
Share of income for year	4,526,000	6,372,000
Dividends	(4,213,600)	(1,114,509)
Adjustment for marketable security valuation....	(1,651,634)	—
Equity in undistributed earnings end of year	$12,244,482	$13,583,716
Cost of investment....	471,900	471,900
Investment end of year	$12,716,382	$14,055,616*

*Reclassified for comparability

Deferred taxes provided	$ 3,911,513	$ 4,295,947
Dividends received by the Company....	$ 2,576,125	$ 828,280

• • • •

In accordance with the requirements of FASB Statement No. 12 "Accounting for Certain Marketable Securities", to reduce the carrying value of the noncurrent marketable equity securities portfolio to market which was lower than cost at December 31, 1975, a valuation allowance was established by a charge to stockholders' equity representing net unrealized losses. This valuation allowance reduced the Company's investment in CBMM $1,652,000, deferred taxes $495,000 and stockholders' equity $1,157,000.

• • • •

RESTATEMENT OF PRIOR PERIODS

If an investee accounted for by the equity method follows accepted accounting practices that differ from those of the investor with respect to marketable equity securities, Statement No. 12 requires those practices to be retained in the consolidated financial statements. Consolidated financial statements of prior periods that have not retained the practices are to be adjusted retroactively according to the manner described in paragraphs 18 and 26 of AICPA Accounting Principles Board Opinion No. 9, "Reporting the Results of Operations."

Two examples are presented of the restatement of prior periods' financial statements.

SEARS, ROEBUCK AND CO.
Statement of Shareholders' Equity

	Year Ended January 31			
	1976	1975	1976	1975*
	(shares)			
Common Stock (including capital in excess of par value)—$1.50 par value, 200,000,000 shares authorized; issued and outstanding as follows:				
Balance, beginning of year	157,827,374	157,343,092	$ 615,806	$ 591,333
Stock options exercised (note 8)	8,100	—	423	—
Issued to Profit Sharing Fund	710,260	484,282	47,998	23,999
Equity in capital transactions of Simpsons-Sears Limited	—	—	726	474
Balance, end of year	158,545,734	157,827,374	664,953	615,806
Retained Income				
Balance, beginning of year (note 2)			4,602,964	4,398,365
Net income (note 2)			522,591	495,898
Dividends to shareholders ($1.85 per share, both years)			(292,373)	(291,299)
Balance, end of year			4,833,182	4,602,964
Unrealized capital gains (losses) on equity investments of Allstate Insurance Company (see pages 26-30):				
Balance, beginning of year (note 2)			(467,497)	(46,418)
Change in unrealized capital gains (losses)			271,803	(421,079)
Balance, end of year			(195,694)	(467,497)
Total Shareholders' Equity			$5,302,441	$4,751,273

*Restated (see note 2, page 19).

Notes to Financial Statements

2. Changes in accounting

In 1975, the company modified certain accounting policies as follows:

• • • •

(c) The company modified its method of accounting for unrealized gains and losses on marketable equity securities to comply with another new financial accounting standard. The company restated its investment in Allstate Insurance Company and the Statement of Shareholders' Equity to include Allstate's unrealized gains and losses on equity securities. This restatement does not affect net income for any period; however, it did decrease the company's investment in Allstate and Shareholders' equity at January 31, 1975 by $467,497,000. At January 31, 1976 this amount had been reduced to $195,694,000.

• • • •

TEXTRON INC.
Consolidated Balance Sheet

	January 3, 1976	December 28, 1974*
• • • •		
Total current assets	971,137	1,012,208
Investments in companies not consolidated, at equity	64,223	58,922
Investments of ARD	29,703	35,180
• • • •		

Shareholders's equity:		
Capital stock:		
$2.08 cumulative convertible preferred, Series A (liquidation value—$153,340,000)	72,475	72,475
$1.40 convertible preferred dividend, Series B	57,081	57,082
Common	7,759	7,759
Capital surplus	67,081	67,095
Retained earnings	602,795	552,720
Unrealized loss on investments	(10,048)	(14,896)
	797,143	742,235
Less treasury stock, at cost	42,652	44,548
Total shareholders' equity	754,491	697,687

Notes to Financial Statements

2. Changes in Accounting

• • • •

Marketable Securities

Statement No. 12 issued by the FASB in December, 1975 requires that, beginning in the fourth quarter of 1975, certain marketable equity securities included in the American Research and Development (ARD) portfolio must be carried at the lower of their aggregate cost or market value. The cumulative amount by which the cost of these investments exceed market value was $949,000 at January 3, 1976. This amount is included in shareholders' equity in the consolidated balance sheet and will not be reflected in income unless realized through sale or recognition of a permanent impairment in value. Prior to the fourth quarter of 1975, ARD investments were carried at cost. See note 3.

In accordance with insurance industry accounting practices, The Security Corporation (Security) and its subsidiaries carry their equity stock investment portfolio at market value with unrealized appreciation or depreciation shown as a component of shareholder's equity. Prior to the issuance of Statement No. 12, Textron did not include such unrealized amounts in recording its investment in Security. Statement No. 12 requires that the accounting practice of Security shall be retained in the consolidated financial statements of Textron and applied retroactively. Accordingly, investments in companies not consolidated and shareholders' equity as previously reported on Textron's 1974 consolidated balance sheet have been reduced by $14,896,000 to reflect the unrealized depreciation in Security's stock investment portfolio.

3. American Research and Development

Investments of Textron's American Research and Development Division (ARD) are principally in venture capital businesses which Textron does not manage. Approximately 80% of the January 3, 1976 portfolio cost represents investments in companies which are less than 20% owned.

ARD portfolio values and income are as follows:

	1975	1974
Portfolio cost:		
Balance at beginning of year	$35,180,000	$37,641,000
Investment additions	1,737,000	539,000
Investment reductions	(6,265,000)	(3,000,000)
Balance at end of year	30,652,000	35,180,000
Less allowance for decline in value of certain marketable securities (see note 2)	949,000*	—
Portfolio stated value at end of year	$29,703,000	$35,180,000
Portfolio market value at end of year (as determined by management, based on market price where available)	$30,591,000	$26,778,000
Portfolio income:		
Dividends and interest	$ 268,000	$ 391,000
Net realized losses (cost determined by specific identity)	(1,582,000)	(375,000)
	$ (1,314,000)	$ 16,000

*Includes gross unrealized gains and gross unrealized losses of $1,608,000 and $2,557,000, respectively.

V

SPECIALIZED INDUSTRY PRACTICES

Certain industries, including investment companies, brokers and dealers in securities, stock life insurance companies, and fire and casualty insurance companies, apply specialized industry accounting practices for marketable securities. FASB Statement No. 12 specifies accounting requirements that are less comprehensive for companies in those industries than are specified for companies in non-specialized industries.

Companies in industries with specialized practices that have carried marketable equity securities at cost are required to carry them at the lower of aggregate cost or market value. However, companies of that type in industries in which either the cost basis or the market basis is an accepted practice may elect the market basis if the election is permissible in that industry.

Statement No. 12 does not alter a company's specialized industry practice for reporting gains and losses, whether realized or unrealized, for marketable equity securities. Companies that do not include unrealized gains and losses on marketable securities in the determination of net income but that do include them in the equity section of the balance sheet are required to disclose (1) gross unrealized gains and gross unrealized losses as of the date of the latest balance sheet presented, and (2) the change in net unrealized gain or loss (the amount by which equity has been increased or decreased as a result of unrealized gains and losses) for each period for which an income statement is presented.

Fifteen examples of accounting for marketable equity securities by companies in industries with specialized accounting practices are presented. The examples are classified by industry. Some of the companies changed their accounting practices to conform with Statement No. 12.

THE E. F. HUTTON GROUP, INC.
Consolidated Statement of Financial Condition

	December 31 1975	1974
Assets		
Cash subject to immediate withdrawal	$ 6,386	$ 12,925
Cash and securities, at market value, segregated under Federal commodity and other regulations	66,321	33,679
Securities, at market value (Note 1):		
U.S. Government	2,324	112
State and municipal	30,553	13,585
Corporate	18,214	9,865
••••		
Stockholders' equity (Notes 7, 8 and 9):		
Common stock, 4,727,141 shares issued	$ 4,727	$ 4,727
Additional paid-in capital	18,351	18,351
Retained earnings	60,457	42,978
	$ 83,535	$ 66,056
Less—Cost of treasury stock	3,695	978
Total stockholders' equity	$ 79,840	$ 65,078

Notes to Financial Statements

1. Summary of Accounting Policies:

••••

Securities and commodities owned are valued at market and the resulting unrealized gains and losses are reflected in income. Securities transactions and related commission income and expenses are recorded in the accounts on settlement date which is generally five business days after trade date. Commodities commission income and related expenses are recorded on trade date.

••••

PAINE WEBBER INCORPORATED
Consolidated Balance Sheet

	September 26 1975	September 27 1974
Assets		
Cash	$ 3,587	$ 6,168
Cash and securities (market value of securities $9,324,000 in 1975; $10,447,000 in 1974) on deposit with clearing associations and segregated under the Commodity Futures Trading Act	11,797	13,698
Receivable from brokers and dealers	35,605	26,957
Receivable from customers	270,853	204,304
Trading account securities—at market value	127,215	68,901
Investment account securities—at market value	15,681	5,547
Securities purchased under agreements to resell—at selling price	46,489	9,463
••••		
Stockholders' Equity		
Series preferred stock, $20 par value, 2,000,000 shares authorized: $1.30 Series A convertible preferred stock, 1,400,000 shares authorized: 1,371,795 shares issued and outstanding	27,436	27,436
Common stock, $1 par value, 10,000,000 shares authorized: 5,338,627 shares issued and outstanding	5,339	5,339
Additional paid-in capital	19,368	19,368
Retained earnings	16,382	6,429
Total stockholders' equity	68,525	58,572

Trading and Investment Account Securities Owned or Sold

Trading and investment account securities are valued at market and unrealized gains and losses are reflected in revenues.

Details of trading account securities follow.

Long security positions (representing dealer inventory securities held for resale to customers):

	1975	1974
	(In thousands of dollars)	
United States Government and Agency securities	$ 93,144	$ 6,195
State and municipal bonds	12,266	16,747
Corporate stocks	3,547	4,562
Corporate debt securities	18,258	41,397
	$127,215	$68,901

Short security positions (securities sold but not yet purchased):

	1975	1974
	(In thousands of dollars)	
United States Government and Agency securities	$ 127	$ 32
State and municipal bonds	398	335
Corporate stocks	1,314	507
Corporate debt securities	4,346	1,419
	$6,185	$2,293

Details of investment account securities follow.

	1975	1974
	(In thousands of dollars)	
Long security positions:		
Corporate stocks	$13,030	$4,997
Corporate debt securities	1,527	442
Options	1,124	108
	$15,681	$5,547
Short security positions:		
Corporate stocks	$12,154	$ 788
United States Government and Agency securities	591	
Corporate debt securities	272	73
Options	914	90
	$13,931	$ 951

COMPANIES ISSUING FIRE AND CASUALTY INSURANCE

CASUALTY INSURANCE SUBSIDIARIES OF INTERFINANCIAL INC.

Balance Sheet

	December 31, 1975	1974 Restated Note A
Assets		
Investments:		
Bonds—principally at amortized cost	$39,185	$33,614
Corporate stocks—at market in 1975; at cost in 1974 (cost—1975, $12,566,966; market—1974, $8,535,478)	3,780	14,034

• • • •

Liabilities and capital		
Claims and unearned premiums	$42,228	$41,969
Accrued expenses and other liabilities	11,808	7,671
Capital—in 1975 adjusted for the net unrealized loss on marketable equity securities of $5,138,000	14,840	18,928

Notes to Financial Statements

Note I: Marketable Equity Securities

At December 31, 1975 the Company and its non-insurance subsidiaries changed the basis for carrying marketable equity securities from cost to lower of aggregate cost or market value. The Company's insurance subsidiaries changed from cost to market value. These changes, required by a recent pronouncement of the Financial Accounting Standards Board, reduced shareholders' equity at December 31, 1975 by $7,641,000 representing the difference in gross unrealized gains ($610,000) and gross unrealized losses ($8,251,000) on marketable equity securities at that date. No tax effect has been recorded with respect to this net unrealized loss.

Because of increases in market prices since December 31, 1975, the net unrealized loss on marketable equity securities had been reduced to $5,601,000 at March 16, 1976.

HARTFORD FIRE INSURANCE COMPANY

Consolidated Balance Sheets

	December 31, 1975	December 31, 1974
Assets		
Investments:		
Bonds and notes, at amortized cost (market value $1,476,821 and $1,275,735)	$1,771,589	$1,613,937
Certificates of deposit, at amortized cost	129,723	78,694
Equity securities (carried at market in 1975 and cost in 1974):		
Common stocks	580,869	798,148
Preferred stocks	28,443	36,278
Redeemable preferred stock, at cost (market value $39,467 and $37,071)	42,353	44,334
Real estate (net of accumulated depreciation of $20,537 and $21,207)	54,693	54,980
	2,607,670	2,626,371

• • • •

Liabilities		
Unpaid claims	$1,431,816	$1,408,594
Unpaid claim expenses	251,971	247,826
Unearned premiums	784,420	780,377
Deferred income taxes (net of $22,445 benefit in 1975 applicable to unrealized loss on marketable equity securities)	91,080	118,749
Other liabilities	129,494	101,351
	2,688,781	2,656,897
Stockholders' Equity		
Preferred stock—Authorized 10,000,000 shares, $1.00 par value Issued 7,670,000 and 9,000,000 shares	7,670	9,000
Common stock—Authorized 40,000,000 shares, $2.50 par value Issued 22,000,000 shares	55,000	55,000
Capital surplus	104,165	110,859
Unrealized loss on marketable equity securities, net of tax benefit	(50,416)	—
Retained earnings	717,318	706,005
Treasury stock, at cost (222,664 common shares)	(6,803)	(6,803)
	826,934	874,061

Consolidated Income and Retained Earnings

	Years ended December 31, 1975	1974
••••		
Income From Operations	54,754	59,409
Net realized investment gains, after applicable income taxes of \$11,081 and \$10,708	21,867	21,771
Decrease (increase) in unrealized loss on marketable equity securities of \$116,566 and (\$224,197) (net of taxes of \$56,172 and tax benefit of \$96,084) in 1975 and 1974 has not been included in reported income.		
••••		

Notes to Financial Statements

Accounting Policies

••••

(b) Hartford invests in equity securities to produce earnings from a combination of dividends and appreciation. Hartford believes that stockholders are entitled to participate currently in the earnings generated by appreciation. Since present accounting rules require the sale of securities in order to record such earnings, Hartford sells securities (on a specific cost identification basis) to realize investment gains.

During 1974, the general economic conditions in the United States and the rest of the free world deteriorated. Inflation and tight money conditions in the United States adversely affected quoted market prices of substantially all common and preferred stocks traded on the major U.S. stock exchanges. Hartford's portfolio, which is composed of a broad spectrum of U.S. companies of the highest quality, was similarly affected. During 1975 there was substantial recovery in Hartford's portfolio which has continued into 1976. In the opinion of management, the unrealized losses currently in the portfolio are temporary, tend to follow the fluctuations in business cycles, and do not represent any indication of a permanent impairment of the stock portfolio. Hartford has and expects to have in the foreseeable future a favorable cash flow and, accordingly, does not anticipate a need to dispose of existing equity securities in order to facilitate future operating growth.

In order to conform with the requirements of the Financial Accounting Standards Board, equity securities are carried at the lower of cost or market (cost of \$677,328,000) at December 31, 1975. To reduce the carrying amount of the equity securities to market at December 31, 1975, a valuation allowance in the amount of \$45,571,000 (after \$22,445,000 tax benefit) was established by a charge to stockholders' equity representing the net unrealized loss. An amount of \$4,845,000, representing net unrealized loss on equity securities held by life insurance subsidiaries was also charged to stockholders' equity. At December 31, 1974, equity securities were not required to be carried at the lower of cost or market at the balance sheet date and were carried at cost. Equity securities had a market value of \$600,935,000 at December 31, 1974. To further conform with the Financial Accounting Standards Board's statement, preferred stocks with specific redemption requirements are not defined as equity securities as of December 31, 1975. Accordingly, the decrease in unrealized loss on equity securities in 1975 excludes these redeemable preferred stocks.

Unrealized gains (losses) pertaining to the equity securities portfolio are shown below (in thousands of dollars):

	March 10, 1976	December 31, 1975	December 31, 1974
Unrealized gains:			
Property and liability companies	\$ 77,897	\$ 70,106	\$ 35,230
Life insurance subsidiaries	323	69	77
Unrealized losses:			
Property and liability companies	(100,909)	(138,122)	(275,984)
Life insurance subsidiaries	(4,227)	(5,359)	(8,956)
Applicable tax effect	7,873	22,890	79,394
	\$ (19,043)	\$ (50,416)	\$(170,239)

In 1975, the tax effect was determined by applying the statutory capital gains rate in effect to the aggregate unrealized gains (losses) at the end of the period. Prior to 1975, the applicable tax effect was determined by applying the capital gains tax rate in effect at the end of each period to the change in market value during the period.

••••

CALIFORNIA LIFE CORPORATION

Consolidated Balance Sheet

	December 31, 1975	December 31, 1974
Assets		
Cash and Investments (Notes 1 and 2):		
Cash (including certificates of deposit; 1975, $725,000; 1974, $1,325,000)	$ 1,833	$ 1,982
Bonds (market value: 1975, $13,159,000; 1974, $10,685,000)	15,784	13,770
Preferred stocks	1,951	2,550
Common stocks	597	1,201

• • • •

	December 31, 1975	December 31, 1974
Shareholders' Equity (Note 6):		
Preferred stock—$10 par value; authorized 2,000,000 shares; none issued		
Common stock—$1.00 par value; authorized 20,000,000 shares; issued 1,036,000 shares	1,036	1,036
Paid-in capital	9,203	9,203
Retained earnings (deficit) (Notes 2 and 4)	185	(400)
Total	10,424	9,839
Less 64,000 common shares held in treasury—at cost	900	900
Total	9,524	8,939
Net unrealized loss on marketable equity securities (Notes 1 and 2)	1,097	
Total Shareholders' Equity	8,427	8,939

Consolidated Statement of Operations and Retained Earnings (Deficit)

	Years Ended December 31, 1975	1974
Revenues (Notes 1 and 2):		
Premiums and considerations:		
Life	$10,528	$11,915
Accident, health and other	18,809	19,242
Investment income and realized losses—net	1,604	1,548

• • • •

Notes to Financial Statements

1. Summary of Accounting Policies:

• • • •

Insurance Operations

• • • •

(4) Investments

Bonds are valued at cost, adjusted for amortization or accretion of premium or discount, determined on a specific identification basis. In conformity with the provisions of Financial Accounting Standard Board Statement No. 12, preferred and common stocks are generally carried at the lower of aggregate cost or market at December 31, 1975. To reduce the carrying amount of these equity securities to market, a valuation allowance is charged against shareholders' equity. At December 31, 1974 these securities were carried at cost. Mortgage and policy loans are valued at the unpaid principal balances. Investments determined to have been permanently impaired have been reduced to estimated value through a charge against income.

2. Life Insurance Subsidiary:

Certain significant accounting and other information pertaining to California Life Insurance Company is as follows:

• • • •

Investment income and net realized losses on sales of investments are summarized as follows:

	1975	1974
Interest on bonds	$1,080,000	$ 973,000
Interest on mortgage loans	269,000	315,000
Dividends	227,000	223,000
Other	89,000	96,000
Total	1,665,000	1,607,000
Less investment expenses	59,000	59,000
Net investment income	1,606,000	1,548,000
Realized losses on investments—net	2,000	1,665,000
Total	$1,604,000	$1,548,000

As described in Note 1, preferred and common stocks were carried on the balance sheet at December 31, 1974 at cost, but are carried at the lower of aggregate cost or market at December 31, 1975. At December 31, 1975 the preferred and common stocks had a cost of $3,646,000; gross unrealized gains were $3,000 and gross unrealized losses were $1,100,000 with respect to the equity securities. At December 31, 1974 preferred and common stocks had a market value of $2,255,000. As of February 27, 1976, the net unrealized loss on marketable equity securities had been reduced by approximately $296,000 from the year end 1975 amount.

• • • •

COMBINED INSURANCE OF AMERICA

Consolidated Statements of Financial Position

	As of December 31	
	1975	1974
Assets		
Cash	$ 5,505	$ 6,705
Investments		
Short-term securities	$ 22,334	$ 25,130
Bonds at amortized cost	293,962	245,928
Preferred stock (1975—market, 1974—cost)	64,442	62,410
Common stock at market value	86,008	64,348

• • • •

Shareholders' Equity		
Capital Stock—$1 par value		
Authorized—28,338,567 shares		
Issued	$ 27,821	$ 27,821
Capital surplus—paid in	7,040	7,040
Net unrealized investment gains (losses)	(8,351)	(10,229)
Mandatory securities valuation reserve	34,497	11,061
Retained earnings	213,241	202,224
Sub-total	$274,248	$237,917
Less cost of treasury stock—1975—1,311,311 shares		
—1974—1,311,268 shares	14,421	14,421
Total Shareholders' Equity	$259,827	$223,496

Consolidated Statements of Shareholders' Equity

	Years ended December 31 1975	1974
Capital Stock	$ 27,821	$ 27,821
Capital Surplus—Paid In	$ 7,040	$ 7,040
Net Unrealized Investment Gains (Losses)		
Balance at January 1	$ (10,229)	$ 4,351
Preferred stock—adjustment to market at December 31, 1975	(15,495)	—
Net increase (decrease) in other unrealized investment gains	17,373	(14,580)
Balance at December 31	$ (8,351)	$ (10,229)
Mandatory Securities Valuation Reserve		
Balance at January 1	$ 11,061	$ 30,225
Appropriation from or (to) retained earnings	23,436	(19,164)
Balance at December 31	$ 34,497	$ 11,061
Retained Earnings		
Balance at January 1	$ 202,224	$ 158,979
Net income	50,371	48,568
Realized investment gains (losses)	272	(10,145)
Cash dividends to shareholders	(16,304)	(14,154)
Appropriation from or (to) mandatory securities valuation reserve	(23,436)	19,164
Other net charges or credits	114	(188)
Balance at December 31	$ 213,241	$ 202,224
Shareholders' Equity Before Deduction of Treasury Stock at December 31	$ 274,248	$ 237,917
Less cost of treasury stock—1975—1,311,311 shares —1974—1,311,268 shares	14,421	14,421
Shareholders' Equity at December 31	$ 259,827	$ 223,496

Notes to Financial Statements

1. Summary of Significant Accounting Principles and Practices

• • • •

Investments

In the consolidated statements of financial position, investments in bonds are generally valued at amortized cost while common stocks are valued at market. Common stocks subject to call options are valued at the lower of the exercise price or market value. In accordance with Statement of Financial Accounting Standards No. 12 (Accounting for Certain Marketable Securities) most preferred stocks at December 31, 1975 are valued at market, while for year ends 1974 and previous years most preferred stocks were valued at cost. Preferred stocks which must be redeemed by the issuing enterprise or are redeemable at the option of the investor are valued at cost. The effect of this change in accounting principles resulted in a $15,495,000 decrease in shareholders' equity at December 31, 1975. The market values of stocks are determined in accordance with the methods prescribed by the National Association of Insurance Commissioners which approximate quoted market values.

Unrealized investment gains or losses are credited or charged to shareholders' equity, net of provision or credit for the Federal income taxes which would be applicable if realized. In this report, net realized investment gains or losses are credited or charged directly to retained earnings net of the applicable income taxes. The Securities and Exchange Commission requires that in filings with it, such as the annual report on Form 10-K, realized investment gains and losses be reflected in net income. The effect of realized investment gains or losses on net income is noted on the accompanying consolidated statements of income.

• • • •

3. Investments

Bonds are generally valued at amortized cost. Bond market values at year end 1975 and 1974 amounted to $250,339,000 and $203,760,000, respectively. Common stocks are valued at market value, except for common stocks subject to call option which are valued at the lower of exercise price or market. The cost basis of all common stocks is $77,428,000 and $74,745,000 at these year ends. Most preferred stocks are valued at market at year end 1975 in accordance with Statement of Financial Accounting Standards No. 12. At December 31, 1974 and prior years most preferred stocks were valued at cost. The market value of all preferred stocks at December 31, 1975 and 1974 is $63,329,000 and $41,132,000. The cost basis of all preferred stocks is $80,950,000 and $63,607,000 at December 31, 1975 and 1974, respectively.

Gross unrealized investment gains and gross unrealized investment losses resulting from valuation changes in marketable securities included in shareholders' equity at December 31, 1975 are $18,959,000 and ($26,911,000), respectively. Unrealized investment gains (losses), net of applicable deferred Federal income taxes, included in shareholders' equity and resulting from valuation changes of marketable securities amounted to $3,774,000 and ($14,379,000) for the years 1975 and 1974, respectively.

Deferred investment income resulting from open or unexpired call options amounted to $514,000 at December 31, 1975. Net investment income from call options is $149,000 for the year 1975. At December 31, 1975, $12,306,000 in carrying value of common stock was encumbered by call options.

● ● ● ●

EQUITABLE LIFE INSURANCE COMPANY OF IOWA

Consolidated Balance Sheets

	December 31 1975	December 31 1974
Assets		
Investments—Notes A and B:		
Bonds—at amortized cost (estimated market value: 1975—$379,679,768; 1974—$338,526,894)	$450,606	$432,469
Preferred stocks—at cost (market: 1975—$7,672,832; 1974—$10,028,728)	10,313	18,305
Preferred stocks—at market (cost—$9,835,856)	5,025	
Common stocks—at market in 1975 (cost—$12,645,484): at cost in 1974 (market—$6,170,405)	9,589	11,496
● ● ● ●		
Stockholders' equity—Notes A, B, and F:		
Common Stock, par value $1 a share:		
Authorized—7,500,000 shares		
Issued—5,000,300 shares, including shares in treasury	5,000	5,000
Additional paid-in capital	6	6
Unrealized depreciation of marketable equity securities	(2,022)	
Retained earnings—including 1975—$33,132,894, 1974—$32,801,501 in excess of stockholders' statutory unassigned surplus	125,921	117,951
	128,906	122,958
Less cost of treasury stock—25,500 shares	242	242
Total stockholders' equity	128,663	122,715

Consolidated Statements of Income

	Year Ended December 31 1975	Year Ended December 31 1974
● ● ● ●		
Income before participating policyholders' share of earnings and realized gains (losses) on investments	16,390	15,261
Participating policyholders' share of earnings in excess of policy dividends paid	5,479	5,187
Income before realized gains (losses) on investments	10,911	10,074
Realized gains (losses) on investments, less participating policyholders' share; 1975—($807,540); 1974—$41,008 (unrealized appreciation [depreciation] of marketable equity securities of $661,299 in 1975 and [$1,293,972] in 1974, net of participating policyholders' share of $2,038,438 and [$3,930,270], respectively, has not been reflected in the consolidated statements of income.)	(279)	13
Net income	$10,631	$10,088

Consolidated Statements of Stockholders' Equity

Years Ended December 31, 1975 and December 31, 1974

	Common Stock	Additional Paid-in Capital	Unrealized Depreciation of Marketable Equity Securities	Retained Earnings	Treasury Stock	Total
Balance at January 1, 1974	$5,000	$6		$109,613		$114,620
Net income for 1974				10,088		10,088
Cash dividends to stockholders ($.35 per share)				(1,750)		(1,750)
Purchase of 25,500 shares of common stock for treasury	—	—		—	($242)	(242)
Balance at December 31, 1974	5,000	6		117,951	(242)	122,715
Net income for 1975				10,631		10,631
Cash dividends to stockholders ($.535 per share)				(2,661)		(2,661)
Unrealized depreciation of marketable equity securities	—	—	($2,022)	—	—	(2,022)
Balance at December 31, 1975	$5,000	$6	($2,022)	$125,921	($242)	$128,663

Notes to Financial Statements

Note A—Significant Accounting Policies

• • • •

Investments

Investments in bonds and mortgage loans on real estate are reported at cost adjusted for amortization of premiums or discounts. Market value of bonds is based on the latest quoted market prices, or where not readily marketable at values which are representative of the market values on issues of comparable maturity and quality.

At December 31, 1975, marketable equity securities are reported at market except for preferred stocks with fixed redemption schedules which are reported at cost. Unrealized appreciation and depreciation is credited or charged directly to stockholders' equity except for permanent declines in market values which are recognized in the determination of net income. At December 31, 1974, marketable equity securities were reported at cost. Investments in policy loans are reported at unpaid principal. Investments in real estate and property and equipment are reported at cost less allowances for depreciation. Realized gains and losses are determined on the basis of specific identification of investments sold and are included in net income.

• • • •

Note B—Basis of Financial Reporting

• • • •

In 1975, the Company changed the basis for carrying its marketable equity securities from cost to market. This change, required by a recent pronouncement of the Financial Accounting Standards Board, reduced stockholders' equity at December 31, 1975 by $2,022,345 (net of participating policyholders' portion of $5,844,444), has no tax effect, and is represented by the difference in gross unrealized appreciation ($215,432) and gross unrealized depreciation ($8,082,221) on marketable equity securities on that date.

Unrealized appreciation (depreciation) of marketable equity securities was $2,699,737 in 1975 and ($5,224,242) in 1974, of which $2,038,438 and ($3,930,270), respectively, was attributable to participating policyholders.

Because of increases in market prices since December 31, 1975, the net unrealized depreciation of marketable equity securities at February 27, 1976, has been reduced by $1,492,821 of which $1,109,164 was attributable to participating policyholders.

• • • •

PREFERRED RISK LIFE INSURANCE COMPANY

Balance Sheets

	December 31 1975	December 31 1974
Assets		
Investments—Note B		
Bonds (market value: 1975—$11,492,436; 1974—$7,956,787)	$12,450	$8,674
Preferred stocks—at market in 1975 (cost—$1,267,875); at cost in 1974 (market—$569,429)	1,087	839
Common stocks—at market in 1975 (cost—$695,029); at cost in 1974 (market—$403,266)	636	572

• • • •

	1975	1974
Stockholders' Equity—Note B		
Common Stock, par value $1 a share:		
Authorized 2,000,000 shares		
Issued and outstanding 1,282,260 shares	1,282	1,282
Capital in excess of par value	3,389	3,389
Unrealized depreciation of marketable equity securities (deduction)—Note B	(238)	
Retained earnings	6,352	4,714
Total Stockholders' Equity	10,785	9,385

Statements of Income

	Year Ended December 31 1975	Year Ended December 31 1974

• • • •

	1975	1974
Income before realized investment losses	1,906	1,631
Realized investment losses [Unrealized depreciation of marketable equity securities (common stocks only in 1974) of $238,924 in 1975 and $169,277 in 1974 has not been reflected in the statements of income]	(11)	(96)
Net income	$1,894	$1,535

Statements of Stockholders' Equity

	Common Stock	Capital in Excess of Par Value	Unrealized Depreciation of Marketable Equity Securities	Retained Earnings
Balance at January 1, 1974	$1,282	$3,389		$3,383
Net income				1,535
Cash dividends to stockholders ($.16 per share)				(205)
Balance at December 31, 1974	1,282	3,389		$4,714
Net income				1,894
Cash dividends to stockholders ($.20 per share)				(256)
Unrealized depreciation of marketable equity securities			($238)	
Balance at December 31, 1975	$1,282	$3,389	($238)	$6,352

Notes to Financial Statements

Note A—Summary of Significant Accounting Policies

Investments

Bonds and mortgage loans on real estate are reported at cost adjusted for amortization of premiums or discounts. At December 31, 1975, preferred and common stocks were reported at market. Unrealized appreciation and depreciation of marketable equity securities is credited and charged directly to stockholders' equity (See Note B). Realized gains and losses on marketable equity securities are determined on the basis of the specific identification of shares sold. Policy loans are reported at unpaid principal. Real estate is reported at the lower of cost or estimated net realizable value. Market value of certain bonds is based on prices which are representative of the market values on issues of comparable yield to maturity. Since the Company generally intends to hold all bonds to maturity, no provision has been made for possible losses on these investments. Realized gains and losses on investments are included in net income.

• • • •

Note B—Basis of Insurance Financial Reporting

• • • •

During 1975, the Company changed its method of accounting for marketable equity securities from cost to market. To reduce the carrying amount of the marketable equity securities to market a valuation allowance in the amount of $238,924 was established by a charge to stockholders' equity representing the unrealized depreciation. At December 31, 1975, the unrealized depreciation of marketable securities was comprised of unrealized appreciation of $60,289 and unrealized depreciation of $299,213.

ZENITH NATIONAL INSURANCE CORP.

Consolidated Balance Sheet

	December 31,	
	1975	1974
Assets		
Marketable Securities:		
Bonds, at amortized cost (market $15,359,000 and $12,277,000)	17,576	15,158
Stocks, at market value (cost $2,462,000 and $2,506,000)	1,869	1,611
• • • •		
Stockholders' Equity		
Preferred Stock, $1 par—shares authorized 1,000,000; none issued	—	—
Common Stock, $1 par—shares authorized 5,000,000; outstanding 1,164,000 (Note 6)	1,164	1,164
Additional Paid-in Capital	7,948	7,948
Deficit	(3,350)	(1,465)
Unrealized Depreciation of Marketable Securities	(577)	(621)
Total Stockholders' Equity	5,185	7,026

Consolidated Statement of Operations

	Year ended December 31,	
	1975	1974
• • • •		
Total expenses	28,479	30,429
Net underwriting income (loss)	1,527	(2,093)
Investment Income—net (Note 7)	1,242	1,140
• • • •		
Income (loss) from continuing operations before realized losses (Note 9)	1,799	(2,004)
Realized losses (Note 7)	(2)	(230)

Consolidated Statement of Stockholders' Equity

Two Years Ended December 31, 1975

	Common stock $1 par	Additional paid-in capital	Retained earnings (deficit)	Unrealized appreciation (depreciation) of marketable securities	Total
Balance at January 1, 1974	$1,164	$7,948	$ 2,272	$(289)	$11,095
Net loss of 1974			(3,737)		(3,737)
Unrealized depreciation of marketable securities, net of $142,000 deferred tax benefit				(332)	(332)
Balance at December 31, 1974	1,164	7,948	(1,465)	(621)	7,026
Net loss for 1975			(1,885)		(1,885)
Unrealized appreciation of marketable securities				336	336
Reversal of deferred tax benefits of prior periods relating to unrealized depreciation (Note 3)				(292)	(292)
Balance at December 31, 1975	$1,164	$7,948	$(3,350)	$(577)	$ 5,185

Summary of Accounting Policies

• • • •

Marketable Securities

Marketable securities are carried at values in accordance with those prescribed by the National Association of Insurance Commissioners. Bonds are carried at amortized cost. Stocks are carried at market value.

Unrealized appreciation or depreciation resulting from the valuation of marketable securities at the balance sheet date is reflected in stockholders' equity, net of applicable income taxes. The cost of securities sold is determined by the "identified certificate" method.

• • • •

Notes to Financial Statements

Note 7—Investment Income

Investment income is summarized as follows:

	1975	1974
Interest on bonds	$ 883,000	$ 818,000
Interest on time certificates of deposit	205,000	137,000
Dividends	166,000	185,000
	1,254,000	1,140,000
Less other investment expenses	12,000	
	$1,242,000	$1,140,000

An analysis of net investment gains and losses is summarized as follows:

	1975	1974
Realized gains (losses):		
Bonds	$ (1,000)	$ (37,000)
Stocks	(1,000)	(193,000)
Total	(2,000)	(230,000)
Unrealized appreciation (depreciation):		
Bonds	664,000	(2,062,000)
Stocks	302,000	(490,000)
Total	966,000	(2,552,000)
Net investment gain (loss)	$ 964,000	$(2,782,000)

The deferred tax benefit of unrealized losses is not provided since realization is not assured. Deferred tax benefits of prior periods on unrealized losses were reversed in 1975.

COMPANIES ISSUING FIRE, CASUALTY, AND LIFE INSURANCE

DURHAM LIFE INSURANCE COMPANY

Consolidated Balance Sheet

	December 31 1975	December 31 1974
Assets		
Bonds—at amortized cost:		
United States Government	$ 11,115	$ 11,099
State and municipal	9,723	8,867
Public utility	41,947	40,265
Industrial and other	56,752	45,286
	119,538	105,519
Preferred stocks—approximately at market in 1975 and at cost in 1974—Note C	35,910	40,175
Common stocks—at market—Note C:		
Investment in a life insurance holding company	23,684	25,302
Other	6,060	4,625

• • • •

Shareholders' equity—Notes B, F, and I:		
Capital Stock, par value $5 a share:		
Authorized 10,000,000 shares		
Issued 2,659,252 shares, including shares in treasury	13,296	13,296
Unrealized investment gains, net of deferred taxes of $2,825,000 in 1975 and $4,875,000 in 1974	14,889	19,704
Retained earnings	64,064	57,367
Cost of Capital Stock in treasury—160,362 shares (deduction)	(2,991)	(2,991)
	89,258	87,376

Consolidated Statement of Operations

	Year Ended December 31 1975	Year Ended December 31 1974

• • • •

Investment income	19,955	18,239
Realized investment gains (Net unrealized investment gains or losses are not reflected in operations—Note C)	98	99

• • • •

Consolidated Statement of Shareholders' Equity

Year ended December 31, 1975, and December 31, 1974

	Capital Stock	Net Unrealized Investment Gains	Retained Earnings	Capital Stock Held in Treasury
Balances at January 1, 1974	$10,641	$29,355	$53,589	$(2,991)
Net income for 1974			8,248	
Decrease in net unrealized investment gains—Note C		(9,651)		
Cash dividends to shareholders—$.72 a share			(1,815)	
5-for-4 stock split—at par value—Note I	2,654		(2,654)	
Balances at December 31, 1974	13,296	19,704	57,367	(2,991)
Net income for 1975			8,695	
Decrease due to change in basis of carrying certain preferred stocks, net of deferred taxes of $2,150,000—Note C		(5,014)		
Increase in net unrealized investment gains—Note C		200		
Cash dividends to shareholders—$.80 a share			(1,998)	
Balances at December 31, 1975	$13,296	$14,889	$64,064	$(2,991)

See notes to consolidated financial statements.

Notes to Financial Statements

Note A—Accounting Policies

• • • •

Investments and property and equipment—Investments in bonds are reported at cost adjusted for amortization of premiums and accrual of discounts; market value was $106,127,289 and $89,976,090 at December 31, 1975 and 1974, respectively. Preferred stocks held by the life company are reported at market value in 1975, except for preferred stocks with sinking fund provisions which are reported at cost. All preferred stocks held by the life company are reported at cost in 1974—see Note C. Preferred stocks held by the fire and casualty subsidiary are reported at market value. Common stocks are reported at market value. Investments in mortgage loans and policy loans are reported at unpaid principal. Realized gains and losses on investments are included in net income. Unrealized investment gains, net of applicable income taxes, are included in shareholders' equity. Property and equipment are reported at cost less allowances for depreciation, which are computed principally on the straight-line method; the allowances for depreciation were $7,052,000 and $6,597,000 at December 31, 1975 and 1974, respectively. The basis for determining cost in computing realized investment gains or losses is specific identification of the cost of the item sold.

• • • •

Note C—Marketable Equity Securities

In compliance with a 1975 pronouncement of the Financial Accounting Standards Board the Company changed its method of reporting preferred stocks without sinking fund provisions held by the life company from cost to market. This resulted in a reduction of $7,164,629, which was charged, after a deferred tax effect of $2,150,000, against the net unrealized investment gains account in shareholders' equity. At December 31, 1975, preferred stocks are reported at $35,910,805, consisting of stocks at market value of $28,051,631 and stocks with sinking fund provisions at cost of $7,859,174. The cost of the regular preferreds was $35,574,432, and the market value of the sinking fund preferreds was $6,780,050. At December 31, 1974, the preferreds were reported at $40,175,881, consisting of stocks held by the life company at cost of $38,060,202 and stocks held by the fire and casualty company at market of $2,115,679. The market value of the life company stocks at that date was $25,590,739, and the cost of the fire and casualty company stocks was $3,010,225.

The cost of common stocks was $4,524,428 at December 31, 1975, and $4,539,991 at December 31, 1974.

At December 31, 1975, gross unrealized gains on marketable equity securities amounted to $26,354,200 and gross unrealized losses to $8,639,364.

The changes in net unrealized investment gains, which do not affect net income, consist of the following:

	1975	1974
Investment in the common stock of a life insurance holding company	$(1,617,969)	$(5,755,469)
Other investments	1,918,061	(8,035,780)
Applicable deferred income taxes	(100,000)	4,140,000
Increase (decrease) in net unrealized investment gains	$ 200,092	$(9,651,249)

AMERICAN INVESTMENT COMPANY

Consolidated Balance Sheet

	1975	1974 (Note 6)
Assets		
Cash	$31,384	$33,117
Marketable securities—at cost, except for $2,510,000 of equity securities stated at market in 1975	58,834	49,107

• • • •

	1975	1974
Stockholders' equity:		
Capital stock:		
Preferred and preference	10,230	10,694
Common	5,496	5,495
Additional paid-in capital	18,124	18,101
Unrealized loss on marketable equity securities	(1,243)	
Retained earnings	34,817	35,026
Total stockholders' equity	67,424	69,316

Statement of Consolidated Stockholders' Equity

For the Years Ended December 31, 1975 and 1974

	Preferred and Preference Stocks	Common Stock	Additional Paid-in Capital	Unrealized Loss on Marketable Equity Securities	Retained Earnings	Total
			(Thousands of dollars)			
Balance, January 1, 1974	$11,157	$5,495	$18,078		$41,190	$75,920
Net income (loss) (Note 6)					(4,335)	(4,335)
Preferred and preference stock redemptions	(463)		23			(440)
Cash dividends:						
5¼% prior preferred $5.25 per share					(74)	(74)
5½% preference $1.375 per share					(519)	(519)
Common $.225 per share					(1,236)	(1,236)
Balance, December 31, 1974	10,694	5,495	18,101		35,026	69,316
Net income					359	359
Preferred and preference stock redemptions	(464)		22			(442)
Common stock options exercised		1	1			2
Unrealized loss on marketable equity securities				$(1,243)		(1,243)
Cash dividends:						
5¼% prior preferred $5.25 per share					(53)	(53)
5½% preference $1.375 per share					(515)	(515)
Balance, December 31, 1975	$10,230	$5,496	$18,124	$(1,243)	$34,817	$67,424

7. Marketable Securities

Marketable securities of the insurance companies are stated at cost (amortized cost with respect to bonds) except for marketable equity securities which are carried at market in 1975, as required by Statement No. 12 of the Financial Accounting Standards Board. Marketable equity securities had a cost of $3,753,000 and a market of $2,510,000 at December 31, 1975. Marketable equity securities on hand at December 31, 1975 had increased in market value to $2,740,000 at January 31, 1976.

To reduce the carrying amount of the marketable equity securities portfolio to market at December 31, 1975, a valuation allowance in the amount of $1,243,000 was established with a corresponding charge to stockholders' equity representing the net unrealized loss.

At December 31, 1974, the marketable equity securities portfolio was not required to be carried at the lower of cost or market at the balance sheet date, and was carried at cost. At December 31, 1974, marketable equity securities had a market value of $2,752,000 and a cost of $4,474,000.

Net realized gains on the sale of marketable equity securities of $161,000 and $214,000 were included in net income for the years 1975 and 1974.

At December 31, 1975 and 1974 the cost and market value of marketable securities was as follows:

	1975		1974	
	Cost	Market	Cost	Market
	(Thousands of dollars)			
Equity securities:				
Common stock	$ 2,347	$ 1,583	$ 3,045	$ 1,961
Preferred stock	1,406	927	1,429	791
Total	$ 3,753	$ 2,510	$ 4,474	$ 2,752
Non-equity securities:				
Preferred stock	$ 1,713	$ 1,583	$ 305	$ 181
Bonds	49,211	40,319	41,440	33,181
Other	5,400	5,400	2,888	2,888
Total	$56,324	$47,302	$44,633	$36,250

In the opinion of management, no permanent impairment of the cost values will be incurred as no significant liquidation of securities is anticipated or required.

GENERAL REINSURANCE CORPORATION

Consolidated Balance Sheet

	December 31	
	1975	1974
Assets		
Marketable securities:		
Bonds, at amortized cost (market: 1975, $709,073,789); 1974, $510,781,774)	$795,709	$613,349
Preferred stocks, at market (cost: 1975, $43,492,503; 1974, $52,036,729)	35,670	34,884
Common stocks, at market (cost: 1975, $181,022,571; 1974, $183,400,822)	192,983	148,780

• • • •

Shareholders' Equity		
Capital (shares authorized, issued and outstanding: 5,445,000, par value $2.00 each)	10,890	10,890
Paid-in capital	5,179	5,179
Unrealized appreciation (depreciation) of investments, net of Federal income tax (1975, $1,246,661; 1974, none)	2,892	(51,773)
Retained earnings	272,658	239,879
Total shareholders' equity	291,620	204,175

Consolidated Statement of Shareholders' Equity

	Year Ended December 31	
	1975	1974
Balance, beginning of year	$204,175	$246,194
Income, excluding realized capital gains (losses)	34,124	32,270
Realized capital gains (losses) net of Federal income taxes	(1,248)	(1,690)
Change in unrealized appreciation (depreciation) of investments:		
Consolidated investments	54,665	(69,379)
Unconsolidated subsidiaries	2,081	(1,314)
Other changes	—	(45)
Dividends to stockholders	(2,178)	(2,178)
Paid-in capital	—	319
Balance, end of year	$291,620	$204,175

Consolidated Statement of Realized Capital Gains (Losses)

	Year Ended December 31	
	1975	1974
Realized capital gain on sale of Swedish Atlas Reinsurance Company Ltd., a wholly owned overseas subsidiary, net of Federal income taxes of $3,093,164	$ 1996	$ —
Realized capital gains (losses) on investments net of Federal income taxes of $(1,173,176) in 1975; none in 1974	(3,244)	(1,690)
Realized capital gains (losses) net of Federal income taxes	$(1,248)	$(1,690)
Realized capital gains (losses) per share	$ (.23)	$ (.31)

Notes to Financial Statements

Note 1—Accounting Policies:

• • • •

(b) Bonds are valued at amortized cost and stocks are included at their market values. Changes in market values of stocks are reflected as unrealized appreciation or depreciation directly in shareholders' equity. Investment income is recognized when earned. Realized capital gains and losses are reflected in a separate statement. The financial statements included herein differ from those filed with the Securities and Exchange Commission in that, the statements filed with the SEC include net realized capital losses of $1,248,136 in 1975 and $1,690,685 in 1974 in a statement of income and that net income is reported for the years ended December 31, 1975 and 1974 in the amounts of $32,875,975 ($6.04 per share) and $30,579,461 ($5.62 per share), respectively.

• • • •

UNIONAMERICA INSURANCE GROUP

Combined Balance Sheet

	December 31	
	1975	1974
Assets		
Investments:		
Bonds (at amortized cost)—Note 3	$93,170	$ 82,179
Preferred stocks (at market in 1975 and cost in 1974)—Note 3	2,671	3,358
Common stocks (at market in 1975 and cost in 1974)—Note 3	1,421	1,373

• • • •

Shareholder's equity		
Preferred stock, $10 par value per share, authorized 5,000 shares; issued 30 shares (aggregate redemption value $3,000,000)	—	—
Common stock, $1 par value per share; authorized 50,000 shares; issued 35,100 shares	35	35
Additional paid-in capital	15,776	15,776
Unrealized depreciation of marketable equity securities —Note 3	(1,148)	—
Retained earnings	15,873	15,363
	30,536	31,174
Treasury stock, at cost (35,000 shares of common stock)	(728)	(728)
Total shareholder's equity	29,808	30,446

Combined Statement of Operations

	Year Ended December 31 1975	1974
• • • •		
Income before income taxes and realized gain or loss on investments	760	1,077
Applicable income taxes (tax credits)—Note 11	334	(1,175)
Income before realized gain or loss on investments	426	2,252
Realized gain (loss) on investments—Note 3	84	(65)
Net income	$ 510	$ 2,187
Unrealized appreciation (depreciation) in value of marketable equity securities—Note 3	$ 613	$ (1,084)

Combined Statement of Shareholder's Equity

	Common Stock	Additional Paid-in Capital	Unrealized Depreciation of Marketable Equity Securities	Retained Earnings	Treasury Stock	Total
Balance December 31, 1973	$35	$15,762	$ —	$13,676	$(728)	$28,745
Net income—1974	—		—	2,187	—	2,187
Dividends paid to parent company	—	—	—	(500)	—	(500)
Capital contributed by parent company	—	14	—	—	—	14
Balance December 31, 1974	35	15,776	—	15,363	(728)	30,446
Net income—1975	—	—	—	510	—	510
Unrealized depreciation of marketable equity securities	—	—	(1,148)	—	—	(1,148)
Balance December 31, 1975	$35	$15,776	$(1,148)	$15,873	$(728)	$29,808

Notes to Financial Statements

1. Summary of Significant Accounting Policies and Basis of Presentation

Other

• • • •

Investment Securities. Bonds are carried at cost, adjusted for the amortization of premiums and discounts. Marketable preferred and common stocks are carried at the lower of their aggregate cost or market value determined at December 31, 1975. At December 31, 1974, such stocks were carried at cost.

At December 31, 1975, the carrying value of such stocks was reduced to market value, resulting in a recognition of unrealized loss of $4,360,000 which, in accordance with the provision of Statement of Financial Accounting Standards No. 12, was charged to shareholders' equity.

• • • •

3. Investment Securities

The cost and market values of investment securities held at December 31, 1975 and 1974 are summarized as follows:

	December 31					
	1975			1974		
	Cost	Market	Unrealized Gain (Loss)—Marketable Equity Securities	Cost	Market	Unrealized Gain (Loss)—Marketable Equity Securities
Insurance Group						
Bonds	$ 93,170	$80,703	$ —	$82,179	$73,238	$ —
Preferred stocks	3,249	2,671	(578)	3,358	2,402	(956)
Common stocks	1,991	1,421	(570)	1,373	568	(805)
	5,240	4,092	(1,148)	4,731	2,970	(1,761)
Mortgage Banking Group						
Restricted marketable securities—Note 1	811	948	—	673	1,009	—
Corporate and Business Services Group						
Common stock						
—Union Bancorp, Inc.	8,394	5,025	(3,369)	8,394	3,990	(4,404)
—Other	32	189	157	300	167	(133)
Other marketable securities	99	99	—	99	99	—
	8,525	5,313	(3,212)	8,793	4,256	(4,537)
Total	107,746	$91,056	$(4,360)	96,376	$81,473	$(6,298)
Valuation allowance	(4,360)			—		
Carrying value	$103,386			$96,376		

The Company has the intent and ability to hold bonds of the Insurance Group until maturity and therefore no provision has been made for unrealized losses.

The following is an analysis of gain or loss on bonds and notes and stocks of the Insurance Group for the years ended December 31, 1975 and 1974:

	(In Thousands) Year Ended December 31			
	1975		1974	
	Bonds and Notes	Stocks	Bonds and Notes	Stocks
Realized gain or (loss)—cost determined by identified certificate	$ 80	$ 4	$ (65)	$ —
Increase (decrease) during year in the difference between market value and cost	(3,526)	613	(6,557)	(1,084)
Net investment gain or (loss)	$(3,446)	$617	$(6,622)	$(1,084)

Income taxes have not been provided nor have tax credits been recognized on realized or unrealized securities gains and losses inasmuch as the Company has a substantial net operating loss carryover for income tax purposes.

GENERAL AMERICAN INVESTORS COMPANY, INC.

Assets and Liabilities

	December 31, 1975
Assets	
Investments, at value (note 1a)	
General portfolio securities (cost $65,628,246)	$86,026
U.S. Government securities (cost $5,999,469)	6,012
Corporate discount notes (cost $4,655,219)	4,655

• • • •

Capital Stock, Surplus and Unrealized Appreciation	
$4.50 Cumulative Preferred Stock, $100 par value (note 3) Authorized 33,770 shares; outstanding 10,049 shares	$ 1,004
Common Stock $1 par value (note 2) Authorized 12,500,000 shares; outstanding (less 13,600 shares in treasury) 7,526,335 shares	7,526
Capital surplus (notes 2 and 3)	59,657
Undistributed realized gain on securities sold (note 2)	6,398
Undistributed income (note 2)	1,893
Unrealized appreciation on investments (note 1c)	20,236
Total	$96,716

Statement of Operations

Year ended December 31, 1975

• • • •

Realized Gain and Change in Unrealized Appreciation on Investments		
Realized gain on general portfolio securities (long-term) (notes 1c and 4)		
Proceeds	$24,427	
Cost (on basis of first-in, first-out)	18,182	$ 6,245
Realized gain on U.S. Government securities ($29,656 short-term)		40
Net realized gain		6,285
Unrealized appreciation on investments (notes 1b and 1c)		
December 31, 1974	3,478	
December 31, 1975	20,236	
Increase in unrealized appreciation		16,757
Net realized gain and increase in unrealized appreciation on investments		$23,043

Statement of Investments

December 31, 1975

Stocks

Shares		Value (note 1a)
Chemical (8.6%)		
30,000	Air Products and Chemicals, Inc.	$ 2,070,000
75,000	Avery Products Corporation	2,043,750
55,000	Loctite Corporate *	797,500
45,000	Nalco Chemical Company	1,361,250
25,000	National Starch and Chemical Corporation	1,112,500
5,000	Raychem Corporation *	935,000
		8,320,000

Consumer Products and Services (3.5%)			
77,000	CFS Continental, Inc.	*	1,193,500
53,500	Ethan Allen, Inc. Class A	*	882,750
75,000	Hartz Mountain Corporation		796,875
28,000	Roper Corporation		465,500
			3,338,625
Data Handling (9.5%)			
41,450†	Access Corporation	††	400,000
20,000	Burroughs Corporation		1,675,000
15,000	International Business Machines Corporation		3,363,750
70,000	NCR Corporation		1,662,500
40,000	Xerox Corporation		2,035,000
			9,136,250
Electrical and Electronics (3.5%)			
75,000	Burndy Corporation		2,456,250
6,000	Harvey Hubbell, Incorporated Class A		168,000
19,000	Harvey Hubbell, Incorporated Class B		543,875
50,000	Spectral Dynamics Corporation of San Diego	*	231,250
			3,399,375
Finance and Insurance (3.2%)			
21,000	Criterion Insurance Company	*	283,500
7,500	General Reinsurance Corporation	*	1,147,500
80,000	Government Employees Insurance Company	*	920,000
100,000	Southland Financial Corporation	*	762,500
			3,113,500
Forest Products (2.6%)			
60,000	Inland Container Corporation		2,557,500
Machinery (Including Components) (5.1%)			
18,000	Caterpillar Tractor Co.		1,255,500
23,500	Chicago Pneumatic Tool Company		602,188
30,000	Deere & Company		1,556,250
70,000	Parker-Hannifin Corporation		1,540,000
			4,953,938
Medical Instruments, Supplies and Services (11.5%)			
35,000	Abbott Laboratories		1,443,750
40,000	Bausch & Lomb Incorporated		1,260,000
35,000	Beckman Instruments, Inc.		1,631,875
50,000	Becton, Dickinson and Company		1,950,000
40,000	Dentsply International Inc.		1,360,000
30,500	Medtronic, Inc.	*	793,000
60,000	Syntex Corporation		1,807,500
50,500	Unitek Corporation		909,000
			11,155,125
Metals and Mining (6.2%)			
80,000	AMAX Inc.		3,780,000
50,000	Hanna Mining Company		2,237,500
			6,017,500
Oil and Natural Gas (15.4%)			
40,000	Amerada Hess Corporation $3.50 Conv. Preferred		1,850,000
21,000	Amerada Hess Corporation		351,750
45,000	Continental Oil Company		2,739,375
90,000	Dome Petroleum Limited		3,060,000
50,000	Imperial Oil Limited Class A		1,112,500
20,000	Marathon Oil Company		827,500
30,000	Superior Oil Company		4,905,000
			14,846,125

Publishing and Printing (5.8%)			
38,500	Booth Newspapers, Inc.	*	933,625
45,000	Gannett Co., Inc.		1,507,500
60,000	Knight-Ridder Newspapers, Inc.		1,755,000
100,000	Media General, Inc. Class A		1,412,500
			5,608,625
Retail and Wholesale Trade (8.2%)			
70,000	Carter Hawley Hale Stores, Inc.		1,750,000
78,000	Fisher Foods, Inc.		819,000
57,500	Lane Bryant, Inc.		711,563
30,000	Mercantile Stores Company, Inc.		1,575,000
70,000	Fred Meyer, Inc. Class A	*	1,076,250
10,000	J. C. Penney Company, Inc.		501,250
60,000	Super Valu Stores, Inc.		1,545,000
			7,978,063
Miscellaneous (5.8%)			
51,500	Dart Industries Inc.		1,442,000
85,000	Premier Industrial Corporation		998,750
70,000	TRW Inc.		1,890,000
45,000	Vetco Offshore Industries, Inc.		1,271,250
			5,602,000
	Total Stocks (88.9%)		86,026,626

• • • •

*On the basis of "over-the-counter" quotations.
†Also 7,150 warrants.
††Restricted security valued at fair value in the opinion of the Directors.

Notes to Financial Statements

1. Significant Accounting Policies:

a. Security Valuation—Securities quoted are valued at last reported sales prices for listed securities traded on the last business day of the period, and at closing bid prices for listed securities not traded on such date and for over-the-counter securities; corporate discount notes are valued at cost which approximates market value; common stock and warrants, not currently quoted, are valued at fair value in the opinion of the Directors.

• • • •

c. Other—As customary in the investment company industry, securities transactions are recorded as of the trade date. Dividend income and distributions to stockholders are recorded as of the ex-dividend dates. Net unrealized appreciation on investments is stated after provision for state and municipal taxes on appreciation, if realized. State and municipal taxes on security profits and state transfer taxes are included as expenses under "Taxes paid and accrued."

AMERICAN DUALVEST FUND INCORPORATED
Statement of Assets, Liabilities and Capital Stock

At December 31, 1975

Assets:

Investments at market value, see statement:

	Cost	Market Value
Common stocks	$18,361	$18,047
Convertible securities	5,013	4,833
Corporate bonds and notes	5,245	5,490
U.S. Government and agencies	6,165	6,112
	$34,786	$34,483

• • • •

Statement of Operations

Year Ended December 31, 1975

• • • •

Realized and Unrealized Gain on Investments:	
Realized gain from securities transactions:	
Proceeds from sales	$31,171
Cost of securities sold	30,332
Net realized gain, identified cost basis—$168,155 on the basis of average cost—Note A	838
Unrealized appreciation (depreciation) of investments:	
Beginning of period	(3,335)
End of period	(302)
Unrealized appreciation	3,032
Net Realized and Unrealized Gain on Investments—Note A	$ 3,871

Investments

At December 31, 1975

Number of Shares or Principal Amount	Security	Market Value (a)	Percentage of Net Assets
Common Stocks			
	Airlines		
25,000	Northwest Airlines, Inc.	$ 575,000	1.76%
18,000	UAL, Inc.	510,750	1.56
		1,085,750	3.32
	Aluminum		
20,000	Kaiser Aluminum & Chemical Corp.	555,000	1.70
	Banking		
17,100	Union Commerce Corp.	102,600	.31
	Chemicals		
10,000	Diamond Shamrock Corp.	533,750	1.63
20,000	Union Carbide Corp.	1,222,500	3.74
		1,756,250	5.37
	Communications		
30,000	American Telephone & Telegraph Co.	1,526,250	4.67
	Consumer Products		
20,000	Gillette Co.	667,500	2.04
15,000	Interco Inc.	581,250	1.78
15,000	Kimberly-Clark Corp.	551,250	1.69
10,000	Philip Morris, Inc.	530,000	1.62
		2,330,000	7.13
	Foods		
5,000	CPC International, Inc.	211,875	.65
12,500	Seven-Up Co.	410,938	1.26
30,000	Tropicana Products, Inc.	757,500	2.32
		1,380,313	4.23
	Housing and Related		
50,000	Carrier Corp.	568,750	1.74
	Insurance		
11,000	American Express Co.	407,000	1.25
33,000	Crum & Forster	808,500	2.47
10,000	INA Corp.	351,250	1.07
		1,566,750	4.79

	Office Equipment		
15,000	Harris Corp.	515,625	1.58
5,000	International Business Machines Corp.	1,121,250	3.43
50,000	Pitney-Bowes, Inc.	725,000	2.22
11,500	Xerox Corp.	585,063	1.79
		2,946,938	9.02
	Oils		
7,500	Continental Oil Co.	456,562	1.40
25,000	Gulf Oil Corp.	512,500	1.57
5,000	Standard Oil Company (Ohio)	343,125	1.05
		1,312,187	4.02
	Paper		
20,000	Fort Howard Paper Co.	577,500	1.77
10,000	Great Northern Nekoosa Corp.	422,500	1.29
		1,000,000	3.06
	Utilities		
11,500	Carolina Power & Light Co.	230,000	.71
15,000	Central & South West Corp.	258,750	.79
15,000	Duke Power Co.	292,500	.90
15,000	Florida Power & Light Co.	403,125	1.23
20,000	Long Island Lighting Co.	317,500	.97
20,000	Pacific Gas & Electric Co.	415,000	1.27
		1,916,875	5.87
	Total Common Stocks	$18,047,663	55.23

• • • •

(a) Market values, unless otherwise noted, represent last sales prices as of December 31, 1975, or, in the absence of recorded sales of listed securities and for securities traded in the over-the-counter market, the average of the closing bid and asked prices as of that date.

• • • •

Notes to Financial Statements

Note A—Summary of Significant Accounting Policies

• • • •

(1) Portfolio valuation: Investments are valued as indicated in the notes following the statement of investments.

(2) Securities transactions and related investment income: Securities transactions are recorded on a trade date basis. Dividend income is recorded on the ex-dividend date and interest income, including amortization of discount on short-term investments, is recorded on the accrual basis. Realized gain and loss from securities transactions is recorded on the basis of identified cost.

• • • •

APPENDIX A

STATEMENT OF FINANCIAL ACCOUNTING STANDARDS NO. 12

ACCOUNTING FOR CERTAIN MARKETABLE SECURITIES

INTRODUCTION AND BACKGROUND INFORMATION

1. There has long been diversity in accounting for marketable securities. Paragraph 9, Chapter 3A, "Current Assets and Current Liabilities," of *Accounting Research Bulletin (ARB) No. 43* (originally adopted as *ARB No. 30* in 1947) narrowed practice somewhat by stating:

> . . . practice varies with respect to the carrying basis for current assets such as marketable securities and inventories. In the case of marketable securities where market value is less than cost by a substantial amount and it is evident that the decline in market value is not due to a mere temporary condition, the amount to be included as a current asset should not exceed the market value.

Chapter 3A of *ARB No. 43* did not, however, deal with the question of whether a write-up of a previous write-down might be permissible to reflect a recovery in the market. *Accounting Principles Board (APB) Opinion No. 18*, "The Equity Method of Accounting for Investments in Common Stock," dealt with accounting for investments by the equity method when the investor has "significant influence" over the investee, thus establishing accounting principles for those investments. In addition, a number of Industry Audit Guides, issued by the AICPA for certain industries, describe specialized accounting practices applied in those industries. At present, some enterprises are carrying marketable securities at cost, some at market (or variations of market), some at the lower of cost or market, and some are applying more than one of those methods to different classes of securities. During 1973 and 1974, there were substantial declines in market values of many securities. As a result, in many enterprises where securities are carried at cost, the carrying amount is in excess of current market value. In other enterprises where carrying amounts were written down to reflect the market decline, the partial recovery in the market in 1975 has given rise to a situation in which securities are being carried at amounts which are below both original cost and current market value.

2. Concern over the lack of definitive guidance in the authoritative literature with respect to certain accounting problems accentuated by these conditions led to requests for the FASB to consider those problems on an urgent basis. The issues raised were submitted to the members of the Board's Screening Committee on Emerging Problems, and their recommendations were weighed by the Board in arriving at its decision to proceed with a project of limited scope, based on the three questions stated in paragraph 3.

3. The Board has concluded that the following questions concerning financial accounting and reporting for marketable securities require resolution as soon as possible:

a) Under what circumstances should marketable equity securities that are carried on a cost basis be written down below cost?
b) Should marketable equity securities that have been written down be written back up based on market recoveries or other criteria?

c) If a parent company and one or more subsidiaries or investees follow different methods of accounting for marketable securities, should any adjustments be made to conform the subsidiaries' or investees' methods of accounting to that of the parent company in consolidated or parent company financial statements?[1]

4. An Exposure Draft of a proposed Statement on "Accounting for Certain Marketable Securities" was issued November 6, 1975, and a public hearing based on the Exposure Draft was held on December 8, 1975. The Board received 272 position papers and letters of comment in response to the Exposure Draft. Twenty presentations were made at the public hearing.

5. This Statement does not apply to not-for-profit organizations[2] or mutual life insurance companies; it does, however, apply to mutual savings banks (see paragraphs 39 and 40) as well as to other for-profit mutual enterprises. This Statement also does not apply to employee benefit plans because that subject is a separate item on the FASB's current agenda.

6. Investments accounted for by the equity method, as described in *APB Opinion No. 18*, are beyond the scope of this Statement except for the provisions of paragraph 18.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Enterprises in Industries Not Having Specialized Accounting Practices with Respect to Marketable Securities

7. For purposes of applying paragraphs 8-13 of this Statement, certain terms are defined as follows:

a) *Equity security* encompasses any instrument representing ownership shares (e.g., common, preferred, and other capital stock), or the right to acquire (e.g., warrants, rights, and call options) or dispose of (e.g., put options) ownership shares in an enterprise at fixed or determinable prices. The term does not encompass preferred stock that by its terms either must be redeemed by the issuing enterprise or is redeemable at the option of the investor, nor does it include treasury stock or convertible bonds.
b) *Marketable*, as applied to an equity security, means an equity security as to which sales prices or bid and ask prices are currently available on a national securities exchange (i.e., those registered with the Securities and Exchange Commission) or in the over-the-counter market. In the over-the-counter market, an equity security shall be considered marketable when a quotation is publicly reported by the National Association of Securities Dealers Automatic Quotations System or by the National Quotations Bureau Inc. (provided, in the latter case, that quotations are available from at least three dealers). Equity securities traded in foreign markets shall be considered marketable when such markets are of a breadth and scope comparable to those referred to above. Restricted stock[3] does not meet this definition.
c) *Market price* refers to the price (see paragraph 7(b)) of a single share or unit of a marketable equity security.
d) *Market value* refers to the aggregate of the market price times the number of shares or units of each marketable equity security in the portfolio. When an entity has taken

---

[1]The term *parent company financial statements* as used in this Statement is limited to those parent company financial statements prepared for issuance as the financial statements of the primary reporting entity.

[2]For this purpose, not-for-profit organizations are those described in the third sentence of paragraph 5 of the Introduction to *ARB No. 43*.

[3]Restricted stock for purposes of this Statement shall mean securities for which sale is restricted by a governmental or contractual requirement except where such requirement terminates within one year or where the holder has the power by contract or otherwise to cause the requirement to be met within one year. Any portion of the stock which can reasonably be expected to qualify for sale within one year, such as may be the case under Rule 144 or similar rules of the Securities and Exchange Commission, is not considered restricted.

positions involving short sales, sales of calls, and purchases of puts for marketable equity securities and the same securities are included in the portfolio, those contracts shall be taken into consideration in the determination of market value of the marketable equity securities.

e) *Cost* refers to the original cost of a marketable equity security unless a new cost basis has been assigned based on recognition of an impairment of value that was deemed other than temporary or as the result of a transfer between current and noncurrent classifications as described in paragraph 10. In such cases, the new cost basis shall be the cost for the purposes of this Statement.

f) The *valuation allowance* for a marketable equity securities portfolio represents the net unrealized loss (the amount by which aggregate costs exceeds market value) in that portfolio.

g) The *carrying amount* of a marketable equity securities portfolio is the amount at which that portfolio of marketable equity securities is reflected in the financial statements of an enterprise.

h) A *realized gain or loss* represents the difference between the net proceeds from the sale of a marketable equity security and its cost.

i) *Net unrealized gain or loss* on a marketable equity securities portfolio represents the difference between the market value of its securities and their aggregate cost at any given date.

8. The carrying amount of a marketable equity securities portfolio shall be the lower of its aggregate cost or market value, determined at the balance sheet date. The amount by which aggregate cost of the portfolio exceeds market value shall be accounted for as the valuation allowance.

9. Marketable equity securities owned by an entity[4] shall, in the case of a classified balance sheet, be grouped into separate portfolios according to the current or noncurrent classification of the securities for the purpose of comparing aggregate cost and market value to determine carrying amount. In the case of an unclassified balance sheet, marketable equity securities shall for the purposes of this Statement be considered as noncurrent assets. The current portfolios of entities that are consolidated in financial statements and that do not follow specialized industry accounting practices with respect to marketable securities shall be treated as a single consolidated portfolio for the comparison of aggregate cost and market value; similarly, the noncurrent portfolios of entities that are consolidated in financial statements and that do not follow specialized industry accounting practices with respect to marketable securities shall be treated as a single consolidated portfolio for the comparison of aggregate cost and market value. The portfolios of marketable equity securities owned by an entity (subsidiary or investee) that is accounted for by the equity method shall not be combined with the portfolios of marketable equity securities owned by any other entity included in the financial statements.[5] However, such an entity is, itself, subject to the requirements of this Statement.

10. If there is a change in the classification of a marketable equity security between current and noncurrent, the security shall be transferred between the corresponding portfolios at the lower of its cost or market value at date of transfer. If market value is less than cost, the market value shall become the new cost basis, and the difference shall be accounted for as if it were a realized loss and included in the determination of net income.

---

[4]For this purpose, marketable equity securities owned by an investee accounted for by the equity method shall not be considered owned by the entity (investor).

[5]This constitutes an exception to paragraph 19 of *APB Opinion No. 18* in those cases in which a subsidiary accounted for under the equity method has a net unrealized gain or loss on a portfolio of marketable equity securities that would serve to offset, in whole or in part, the net unrealized gain or loss on a comparable portfolio of marketable equity securities of the parent or consolidated entity. If the subsidiary were consolidated and its portfolios were combined with comparable portfolios of other entities in the consolidation in accordance with this paragraph, a different effect on consolidated net income would be produced, as compared with the equity method.

11. Realized gains and losses shall be included in the determination of net income of the period in which they occur. Changes in the valuation allowance for a marketable equity securities portfolio included in current assets shall be included in the determination of net income of the period in which they occur. Accumulated changes in the valuation allowance for a marketable equity securities portfolio included in noncurrent assets or in an unclassified balance sheet shall be included in the equity section of the balance sheet and shown separately.

12. The following information with respect to marketable equity securities owned shall be disclosed either in the body of the financial statements or in the accompanying notes:

a) As of the date of each balance sheet presented, aggregate cost and market value (each segregated between current and noncurrent portfolios when a classified balance sheet is presented) with identification as to which is the carrying amount.
b) As of the date of the latest balance sheet presented, the following, segregated between current and noncurrent portfolios when a classified balance sheet is presented:
    i) Gross unrealized gains representing the excess of market value over cost for all marketable equity securities in the portfolio having such an excess.
    ii) Gross unrealized losses representing the excess of cost over market value for all marketable equity securities in the portfolio having such an excess.
c) For each period for which an income statement is presented:
    i) Net realized gain or loss included in the determination of net income.
    ii) The basis on which cost was determined in computing realized gain or loss (i.e., average cost or other method used).
    iii) The change in the valuation allowance(s) that has been included in the equity section of the balance sheet during the period and, when a classified balance sheet is presented, the amount of such change included in the determination of net income.

13. An enterprise's financial statements shall not be adjusted for realized gains or losses or for changes in market prices with respect to marketable equity securities when such gains or losses or changes occur after the date of the financial statements but prior to their issuance, except for situations covered by paragraph 21. However, significant net realized and net unrealized gains and losses arising after the date of the financial statements, but prior to their issuance, applicable to marketable equity securities owned at the date of the most recent balance sheet shall be disclosed.

Enterprises in Industries Having Specialized Accounting Practices with Respect to Marketable Securities

14. Certain industries apply specialized industry accounting practices with respect to marketable securities. Such industries include investment companies, brokers and dealers in securities, stock life insurance companies, and fire and casualty insurance companies. Except for the requirements in paragraphs 15, 21, and 22, this Statement does not alter any industry's specialized accounting practices. Paragraphs 15, 17, and 19 deal with marketable equity securities as that term is defined in paragraph 7. Paragraphs 16, 18, and 20-22 deal with marketable securities as that term is used in the particular industries concerned, including, but not limited to, marketable equity securities.

15. Entities that carry marketable equity securities at cost shall hereafter carry them at the lower of their aggregate cost or market value.[6] In making this determination, the provisions of paragraphs 7-9 shall be applied with the exception of the third sentence of paragraph 9. The portfolios of entities that are consolidated in financial statements and that follow the same specialized industry accounting practices with respect to marketable equity securities shall be

---

[6]This does not preclude entities in industries in which either the cost basis or the market basis is an accepted specialized practice from electing the market basis where such election is permissible in that industry. In such an election, the provisions of paragraphs 15-17 of *APB Opinion No. 20,* "Accounting Changes," shall not apply.

treated as a single portfolio for the comparison of aggregate cost and market value. This Statement does not alter any entity's specialized industry practice for reporting gains and losses, whether realized or unrealized, for marketable equity securities.

16. Entities that do not include unrealized gains and losses[7] on marketable securities in the determination of net income but that do include them in the equity section of the balance sheet shall disclose the following information, either in the body of the financial statements or in the accompanying notes:

a) Gross unrealized gains and gross unrealized losses as of the date of the latest balance sheet presented.
b) Change in net unrealized gain or loss (the amount by which equity has been increased or decreased as a result of unrealized gains and losses) for each period for which an income statement is presented.

17. An enterprise's financial statements shall not be adjusted for realized gains or losses or for changes in market prices with respect to marketable equity securities when such gains or losses or changes occur after the date of the financial statements, but prior to their issuance, except for situations covered by paragraph 21. However, significant net realized and net unrealized gains and losses arising after the date of the financial statements, but prior to their issuance, applicable to marketable equity securities in the portfolio at the date of the most recent balance sheet shall be disclosed.

Enterprises That Include Entities Whose Accepted Accounting Practices Differ with Respect to Marketable Securities

18. If an investee accounted for by the equity method or a subsidiary follows accepted accounting practices that are different from those of the parent or investor with respect to marketable securities, those practices shall be retained in the consolidated or parent company financial statements in which those entities are included. As an exception to this requirement, if it is the practice of the parent or investor to include realized gains and losses in the determination of net income, or would so include them if present, the accounting treatment of a subsidiary or an investee that does not follow such practice shall be conformed to that of the parent or investor in that particular respect in consolidated or parent company financial statements.

19. If the parent company in a consolidation follows specialized industry accounting practices with respect to marketable securities but two or more consolidated subsidiaries do not (and hence are subject to the provisions of paragraphs 8-13 of this Statement), the current and noncurrent portfolios of marketable equity securities of such subsidiaries shall be consolidated as separate current and noncurrent portfolios in the manner provided in paragraph 9, exclusive of the portfolios of the parent company, for the purpose of determining carrying amounts in accordance with paragraph 9. The information required by paragraph 12 shall be disclosed in the consolidated financial statements with respect to such subsidiaries.

20. If the consolidated financial statements reflect more than one accepted practice of accounting for marketable securities, the disclosures required by this Statement and those encompassed by specialized industry practice, as applicable, shall be disclosed either in the body of the financial statements or in the accompanying notes for the marketable securities accounted for under each such practice.

Decline in Market Value Is Assessed to Be Other Than Temporary

21. For those marketable securities for which the effect of a change in carrying amount is included in stockholders' equity rather than in net income (including marketable securities in

[7]For the purposes of paragraph 16, unrealized gains and losses shall have the same meaning as is presently accepted in the particular industry's specialized accounting practice.

unclassified balance sheets), a determination must be made as to whether a decline in market value below cost as of the balance sheet date of an individual security is other than temporary.[8] If the decline is judged to be other than temporary, the cost basis of the individual security shall be written down to a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in market value.

Income Taxes

22. Unrealized gains and losses on marketable securities, whether recognized in net income or included in the equity section of the balance sheet, shall be considered as *timing differences*, and the provisions of *APB Opinion No. 11*, "Accounting for Income Taxes," shall be applied in determining whether such net unrealized gain or loss shall be reduced by the applicable income tax effect. A tax effect shall be recognized on an unrealized capital loss only when there exists assurance beyond a reasonable doubt that the benefit will be realized by an offset of the loss against capital gains.

Effective Date and Transition

23. The provisions of this Statement, other than those of paragraph 18, shall be effective for financial statements for annual and interim periods ending on or after December 31, 1975.[9] If initial application of this Statement necessitates establishment of a valuation allowance for a marketable equity securities portfolio included in current assets, the amount thereof shall be included in the determination of net income for the period in which this Statement is initially applied. If initial application of this Statement necessitates establishment of a valuation allowance for a marketable equity securities portfolio included in noncurrent assets or in an unclassified balance sheet, the amount thereof shall be reflected separately in stockholders' equity as of the end of the period in which this Statement is initially applied. For initial application of this Statement, the provisions of paragraph 10 shall not apply to transfers between current and noncurrent classifications made as of or before December 31, 1975.[10] Financial statements for annual and interim periods ending before December 31, 1975[11] shall not be restated except as stated below. The provisions of paragraph 18 of this statement shall be effective for financial statements for annual and interim periods ending on or after December 31, 1975.[12] Those provisions shall be applied retroactively by prior period adjustment (described in paragraphs 18 and 26 of *APB Opinion No. 9*, "Reporting the Results of Operations"). When prior period financial statements or financial summaries or other data derived therefrom are presented, they shall be restated to conform to those provisions.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the affirmative votes of five members of the Financial Accounting Standards Board. Messrs. Litke and Sprouse dissented.

Mr. Litke and Mr. Sprouse dissent primarily because this Statement *requires* some enterprises in industries not having specialized accounting practices to recognize unrealized gains in the

[8]For a recent discussion of this subject, see the Auditing Interpretation published by the staff of the Auditing Standards Division. AICPA, "Evidential Matter for the Carrying Amount of Marketable Securities," in *The Journal of Accountancy*, April 1975.

[9]For enterprises having fiscal years of 52 or 53 weeks instead of the calendar year, this Statement shall be effective for financial statements for periods ending in late December 1975.

[10]See footnote 9.

[11]See footnote 9.

[12]See footnote 9.

determination of net income of the period in which they occur and *prohibits* other similar enterprises from recognizing unrealized gains in circumstances that are in substance identical. In their view, recognition of a gain should depend on underlying economic circumstance—in this case whether or not a security's market value has increased. Under this Statement, however, recognition of an unrealized gain in the determination of net income depends on accounting irrelevancies such as (1) whether the security is classified in the balance sheet as a current asset or a noncurrent asset, (2) whether unrealized losses on marketable securities had previously been recognized in net income of prior periods, and (3) whether in a given accounting period an enterprise has unrealized losses in some securities that offset unrealized gains in others. Mr. Litke and Mr. Sprouse hold that accounting for similar circumstances similarly and for different circumstances differently is an important objective in establishing financial accounting standards. This Statement, in their judgment, ignores that objective.

Mr. Litke and Mr. Sprouse believe that accounting for marketable securities held as current assets on a portfolio basis has significant defects. In comparing the aggregate cost and market value of a portfolio, the Statement calls for unrealized gains to be recognized to the extent of any unrealized losses. In this way, unrealized gains may be recognized implicitly by some enterprises while the implicit or explicit recognition of similar unrealized gains by other enterprises is precluded. Also, reporting the carrying amount of a portfolio at the lower of the aggregate cost or market value may be deceptive because it may suggest that all unrealized losses have been recognized in the period in which market values have declined. Unrealized losses that are not recognized at the end of a period because they are offset by unrealized gains on other securities in the portfolio may have to be recognized in a future period when a component of the portfolio is sold. That could be the effect even in the absence of any further changes in market value. As a result, like the cost method it is intended to supplant, the lower of cost or market rule applied on a portfolio basis may cause losses from declines in market value to be recognized in the period of sale rather than in the period in which the loss in market value occurs.

Mr. Sprouse agrees that the scope of this Statement is properly confined to resolution of the three questions stated in paragraph 3. He also agrees that current assets should not be carried at amounts in excess of their net realizable value, that in the case of marketable equity securities the best measure of net realizable value is their current market value, and that unrealized losses on marketable securities classified as current assets should be included in the determination of net income of the period in which they occur. However, since the Board concluded that it is not feasible at this time to consider comprehensively the recognition of unrealized gains on marketable equity securities, in the interest of equity and comparability among enterprises Mr. Sprouse believes that no recognition of unrealized gains is preferable to the partial and arbitrary recognition required by this Statement.

Mr. Litke believes that marketable securities should not be carried in amounts in excess of their net realizable value and that the best measure of net realizable value is their current market value. He believes that this Statement should require that all marketable equity securities be carried at market value in the balance sheet. While his inclination at this time would be to recognize unrealized market value changes in the determination of net income, he believes that the Board should not take that step in this Statement given the limited scope of the project. In Mr. Litke's opinion, the solution to the emerging problem of accounting for marketable equity securities would be for the financial statements to include in income only: (1) realized gains and losses resulting from exchange transactions, and (2) provisions to recognize the effect of permanent impairment of the security's value. Under this solution, he believes all unrealized gains and losses on both current and noncurrent marketable equity securities should be added to or deducted from stockholders' equity, except that the effect of permanent impairment would be deducted from income.

Members of the Financial Accounting Standards Board:

Marshall S. Armstrong, *Chairman*
Oscar S. Gellein
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
Walter Schuetze
Robert T. Sprouse

Appendix A

BASIS FOR CONCLUSIONS

24. This Appendix discusses factors deemed significant by members of the Board in reaching the conclusions in this Statement, including alternatives considered and the reasons for accepting some and rejecting others.

Scope

25. The three questions which the Board addressed as constituting financial reporting problems requiring early resolution are those listed in paragraph 3. Questions (a) and (b) relate to the determination of carrying amount for marketable equity securities, whereas question (c) relates to the issue of conformity in consolidated or parent company financial statements of different methods of accounting with respect to all marketable securities, whether or not they are equity securities.

26. Because of the urgency of resolving these questions within a limited time frame, the Board concluded that the scope of the project should be limited essentially to the questions as presented. Although a number of respondents objected to the short exposure period and the proximity of the proposed effective date, the Board determined that the problems should be resolved for application in 1975. As stated in paragraph 2, the requests that the Board deal with the problems had indicated that such a timely answer was needed. On the basis of available information, including that obtained at the public hearing and in position papers and letters of comment, the Board concluded that it could make an informed decision on the questions as presented and that the effective date and method of transition specified herein are advisable.

27. The Board is mindful of the fact that enterprises in certain industries apply specialized accounting practices presently accepted in those industries. The Board concluded that consideration of questions (a) and (b) with respect to those particular industries should be limited to the enterprises within those industries that carry marketable equity securities on the basis of cost. The alternative bases for carrying marketable equity securities (e.g., market value, appraised value, fair value) which are permitted in certain specialized industry accounting practices with respect to marketable securities have not been considered by the Board and are not altered by this Statement. The Board further concluded that it would not, as a part of this project, examine or change specialized industry practice for reporting gains and losses, whether realized or unrealized, for marketable securities. To do so would expand the scope of the project in that consideration of the fundamental issues that led to the adoption of those specialized practices would be required. This, the Board decided, could not be done in the limited time available for the completion of this project.

28. For the reasons discussed in paragraph 27, the "Standards of Financial Accounting and Reporting" of this Statement contain separate provisions for two categories of enterprises: those in industries not having specialized accounting practices with respect to marketable securities, and those in industries having such specialized accounting practices.

Enterprises in Industries Not Having Specialized Accounting Practices with Respect to Marketable Securities

29. In considering questions (a) and (b) of paragraph 3 the Board noted that the questions pertain to marketable equity securities carried on a cost basis. The Board's conclusion that the lower of cost or market should apply in the determination of carrying amount for such securities was based on the following factors:

a) The Board excluded from its consideration market value alone as the determinant of carrying value. Consideration of that alternative would raise pervasive issues concerning the valuation of other types of assets, including the concept of historic cost versus current or realizable value. The Board concluded that it could not examine these conceptual issues in a project of such limited scope.
b) The Board noted that continuance of original cost as the carrying amount of a portfolio of marketable equity securities when its market value is lower has the effect of deferring recognition of the decline in the realizable value of such securities based on the expectation of a future recovery in market value which may or may not occur. Because of the uncertainty of such future recovery, the Board concluded that original cost is not a proper determinant of carrying amount for marketable equity securities when market value is below cost. A number of respondents advanced the argument that, in the case of securities held as long-term investments, a decline in market value viewed as temporary should not be reflected in net income. While not necessarily accepting this argument, the Board took into account the fact that this argument has considerable support in current practice, and that the Auditing Interpretation referred to in footnote 8 is consistent with it. The Board concluded that the conceptual question of whether such differences should or should not be included in income could not be dealt with in this project, and hence no such requirement should be made at this time. However, the Board concluded that a decline in market value below cost should in all cases be reflected in the balance sheet and when such securities are classified as current assets, the decline in market value below cost should enter into the determination of net income. In the case of current assets, it is the Board's view that the realization of the loss in value of the securities should be regarded as imminent and therefore should be recognized in the determination of net income.
c) In adopting the lower of cost or market as the determinant for carrying amount, the Board required that when writedowns have been made because the market value of the portfolio has dropped below cost, if market value subsequently rises, the write-down be reversed to the extent that the resulting carrying amount does not exceed cost. The Board does not regard the reversal of the write-down as representing recognition of an unrealized gain. Rather, the Board views the write-down as establishing a valuation allowance representing the estimated reduction in the realizable value of the portfolio, and it views a subsequent market increase as having reduced or eliminated the requirement for such an allowance. In the Board's view, the reversal of the write-down represents a change in an accounting estimate of an unrealized loss (see paragraph 2 of *FASB Statement No. 5*, "Accounting for Contingencies," and paragraph 10 of *APB Opinion No. 20*).

30. The Exposure Draft required that all changes in the carrying amounts of the marketable equity securities portfolio be reflected in income currently and made no distinction in that regard between the current or noncurrent classifications of such securities. Some respondents favored the separation of the single portfolio called for by the Exposure Draft into current and noncurrent portfolios with the change in carrying amount for the noncurrent portfolio to be reflected in equity rather than in income. They argued that fluctuations in the market value of long-term investments should not be reflected in income and to do so would cause distortions which would not be

understood by investors. While not necessarily agreeing with these arguments, for the reasons discussed in paragraph 29(b), the Board decided not to require in this Statement that declines in the market value below cost of noncurrent marketable equity securities be reflected in net income. In reaching this decision, the Board recognized that the present concepts of income require authoritative clarification with respect to the recognition of unrealized gains and losses on long-term assets. Such clarification, the Board noted, is beyond the scope of this Statement. For these reasons, the Board concluded that marketable equity securities classified as noncurrent assets should constitute a separate portfolio from those securities classified as current assets for the determination of carrying amount, and that changes in the carrying amount of the noncurrent portfolio should be reflected in the equity section of the balance sheet rather than included in income, provided that the decline in market value is assessed as temporary.

31. An issue inherent in the determination of carrying amount for marketable equity securities was whether the lower of cost or market method adopted by the Board should be applied on the basis of individual security holdings or on a portfolio basis. In deciding to require application on a portfolio basis (with the exceptions noted in paragraph 9), the Board considered the following factors: Many enterprises regard their portfolios of marketable equity securities (excluding long-term investments accounted for under the equity method) as collective assets. A requirement that the application of lower of cost or market be made on an individual security basis would, in the Board's view, be unduly conservative and at variance with the manner in which enterprises generally view their investment in marketable equity securities. The Board recognized that the application of the criterion on a portfolio basis may be regarded as having the effect of offsetting the unrealized losses on one security with unrealized gains on another. However, the Board agrees with those respondents who regard the current and noncurrent portfolios of marketable equity securities each as collective assets, hence the determination of the carrying amount on a collective (portfolio) basis is in the Board's view appropriate despite the offsets referred to. The disclosures required by paragraph 12(b) are intended to inform as to the extent to which such offsets exist in the portfolio.

32. Paragraph 30 discussed the reasons for the Board's decision to change from a single portfolio basis as provided by the Exposure Draft to separate portfolios for current and noncurrent assets. The Exposure Draft noted that such a separation of portfolios would provide opportunities for transfers between portfolios simply by changing classifications and that such transfers could result in significant changes in net income. The Board had this feature in mind in requiring that transfers between the current and noncurrent portfolios be accounted for in the manner prescribed by paragraph 10. This has the effect of accounting for an unrealized loss at the date of transfer in the same manner as if it had been realized, thus reducing the incentive to cause significant changes in income by transferring securities between portfolios. The Board recognized, however, that the above requirement would not be effective in the case of a transfer from noncurrent to current classifications of a security having an excess of market value over cost which would serve to offset a reverse situation in the current portfolio, thus affecting the determination of net income. However, as mentioned in paragraph 31, the disclosures required by paragraph 12(b) should assist users of financial statements in assessing the effects of such transfers.

33. The definition of "equity security" in the Exposure Draft included convertible bonds. Many respondents believed that such inclusion was in conflict with *APB Opinion No. 14*, "Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants." It was pointed out further that the market sometimes values a convertible bond primarily on its equity characteristics and at other times primarily on its debt characteristics. The Board concluded that it was impractical to apply criteria under which a convertible bond might in some time intervals come under the definition and at other times be excluded. Accordingly, the Board decided that convertible bonds, and, for consistency, convertible preferred stock with redemption requirements, would be excluded from the definition of equity securities.

34. A number of respondents asked for clarification of what was encompassed by the term "restricted stock" with respect to the statement in the Exposure Draft that restricted stock did not meet the definition of "marketable." Footnote 3 of this Statement is intended to provide the requested clarification. The Board's decision to consider restricted stock as meeting the definition of marketable where the restriction terminates or can be terminated by the holder within one year is based on the view that current market value is relevant in applying the lower of cost or market determination to such securities, whereas in the case of longer term restrictions, the application of current market value is of lesser relevance.

35. Paragraph 9 provides, as did the Exposure Draft, that "The portfolios of marketable equity securities owned by an entity (subsidiary or investee) that is accounted for by the equity method shall not be combined with the portfolios of marketable equity securities owned by any other entity included in the financial statements.[5]" Some respondents were of the opinion that the portfolio(s) of unconsolidated subsidiaries accounted for by the equity method should be so combined, especially in the case of 100 percent owned subsidiaries, and that failure to do so would be contrary to paragraph 19 of *APB Opinion No. 18*. Some of the respondents expressing this view acknowledged that there were both conceptual and mechanical problems involved in implementing this recommendation, but none offered specific suggestions for resolving them. The Board noted in the Exposure Draft and in footnote 5 of this Statement that the procedure called for constitutes an exception to paragraph 19 of *APB Opinion No. 18*. The Board rejected the recommendation that the portfolios of equity method subsidiaries be combined with others, because to do so could produce illogical results either with respect to the carrying amount of marketable securities as reflected in the consolidated balance sheet, or the carrying amount of the equity method subsidiary as reflected in the same balance sheet.

Enterprises in Industries Having Specialized Accounting Practices with Respect to Marketable Securities

36. Paragraph 14 states that, with the exception of paragraphs 15, 21, and 22, this Statement does not alter any industry's specialized accounting practices with respect to marketable securities.

37. Paragraph 15 requires that entities that carry marketable equity securities at cost shall hereafter carry them at the lower of their aggregate cost or market value with the following exception: entities in industries whose specialized accounting practices permit market value as an acceptable alternate carrying basis may elect that basis. The cost basis is no longer acceptable for determining carrying amount for marketable equity securities and is replaced by the lower of aggregate cost or market value.

38. The Board's decision to replace the cost basis with the lower of cost or market basis in industries having specialized accounting practices took into account the following factors:

a) Having concluded that the cost basis should be replaced in all enterprises in industries with nonspecialized accounting practices, the Board could find no justification for maintaining cost as a basis for marketable equity securities in the other industries.
b) As stated in paragraph 27, this Statement does not alter specialized industry practice for reporting gains and losses on marketable securities because to do so would involve a reconsideration of fundamental issues in those industries. However, a change in the carrying basis for marketable equity securities does not, in the Board's view, necessitate such a reconsideration.
c) Elimination of cost as a carrying basis for marketable equity securities in the industries having specialized accounting practices serves to reduce some of the disparity in practice among those industries as well as with industries not having specialized accounting practices.

Applicability

39. Numerous responses from the mutual savings bank industry urged that mutual savings banks be excluded from the scope of this Statement. The principal arguments advanced were: mutual savings banks are regulated and, in some states, are required to carry marketable securities at cost; the exclusion of not-for-profit organizations should apply to mutual savings banks; the element of mutuality (absence of shareholders) applies equally to these organizations as it does to mutual life insurance companies. The Board did not find these arguments persuasive. When mutual savings banks, which are in an industry not having specialized accounting practices, present financial statements purporting to be in conformity with generally accepted accounting principles, the fact that they are regulated or that they do not have shareholders does not, in the Board's view, justify different accounting for marketable equity securities from that required to be followed by other entities not having specialized accounting practices. Accordingly, the provisions of this Statement apply to mutual savings banks, as well as to other for-profit mutual enterprises, except mutual life insurance companies.

40. Mutual life insurance companies were excluded from the scope of this Statement because, unlike stock life insurance companies (see paragraph 14), there is disagreement as to whether generally accepted accounting principles exist for mutual life insurance companies.[13] This coupled with the complexity of some of the issues involved in life insurance accounting caused the Board to conclude that it could not resolve these questions within this project. On the other hand, mutual savings banks, which are not excluded from the scope of this Statement, do present financial statements prepared in conformity with generally accepted accounting principles and there are no complex related accounting issues involved as is the case with mutual life insurance companies.

41. The Exposure Draft proposed that the Statement be applied retroactively by prior period restatement. That method of transition was proposed on the premise that it would afford maximum comparability among financial statements. The Board has obtained information, subsequent to the issuance of the Exposure Draft, that a number of companies have in past years made substantial reclassifications of marketable equity securities as between current and noncurrent assets. With the Board's decision to provide for separate portfolios of current and noncurrent marketable equity securities with different accounting for changes in carrying value of the two portfolios, the number of and seemingly divergent bases for reclassifications that have occurred in recent years would, in the case of retroactive restatement, result in less rather than more comparability. The new requirement that transfers between current and noncurrent portfolios be accounted for in a manner to treat reductions in market value below cost as realized losses at the date of transfer would, if applied retroactively, accentuate this effect. For these reasons, the Board concluded that the interests of users of financial statements would best be served by making the Statement effective December 31, 1975[14] (except for paragraph 18 for which retroactive application is still required).

Appendix B

ILLUSTRATION OF DISCLOSURES REQUIRED BY PARAGRAPH 12 OF THIS STATEMENT

42. The following example illustrates the disclosure requirements of paragraph 12 for an enterprise having a classified balance sheet. For purposes of this illustration it is presumed that the only marketable securities that the enterprise owns are marketable equity securities as defined in paragraph 7. The illustration does not encompass all possible circumstances that may arise in connection with the disclosure requirements, nor does it indicate the Board's preference for a particular format.

---

[13]See the Preface to *AICPA Industry Audit Guide*, "Audits of Stock Life Insurance Companies."
[14]See footnote 9.

Computational Information

The details on the following pages pertain to marketable equity securities owned at December 31:

	1975			1974		
	Cost	Market	Unrealized Gain (Loss)	Cost	Market	Unrealized Gain (Loss)
In Current Assets:						
Security A	$100,000	$100,000	$ —	$200,000	$250,000	$ 50,000
B	200,000	150,000	(50,000)	300,000	250,000	(50,000)
C	200,000	175,000	(25,000)	200,000	150,000	(50,000)
D	150,000	100,000	(50,000)	150,000	200,000	50,000
E	50,000	100,000	50,000	50,000	75,000	25,000
F	200,000	225,000	25,000	—	—	—
Total of Portfolio	$900,000	$850,000	$ (50,000)	$900,000	$925,000	$ 25,000
Valuation Allowance—Current			$ (50,000)			Not Applicable
In Noncurrent Assets:						
Security G	$300,000	$200,000	$(100,000)	$300,000	$100,000	$(200,000)
H	100,000	190,000	90,000	100,000	250,000	150,000
I	250,000	150,000	(100,000)	250,000	150,000	(100,000)
Total of Portfolio	$650,000	$540,000	$(110,000)	$650,000	$500,000	$(150,000)
Valuation Allowance—Noncurrent			$(110,000)			Not Applicable

During 1975 the following sales of securities took place. (There were no sales of securities in 1974.):

	Net Proceeds of Sale	Cost	Realized Gain (Loss)
Security A	$125,000	$100,000	$ 25,000
Security B	65,000	100,000	(35,000)
	$190,000	$200,000	$(10,000)

The valuation allowances required at December 31, 1975 are as follows:

	Charged Against Income	Charged Against Equity
In Current Assets:		
Cost $900,000 less market $850,000	$50,000*	
In Noncurrent Assets:		
Cost $650,000 less market $540,000		$110,000*

*No tax effect was recognized because there is no assurance beyond a reasonable doubt that the benefit will be realized by an offset of the loss against capital gains.

Disclosure Requirements

BALANCE SHEET

	December 31, 1975	December 31, 1974
Current Assets		
Marketable equity securities, carried at market in 1975 and at cost in 1974 (Note 1)	$ 850,000	$900,000
Noncurrent Assets		
Marketable equity securities, carried at market in 1975 and at cost in 1974 (Note 1)	540,000	650,000
Stockholders' Equity		
Net unrealized loss on noncurrent marketable equity securities (Note 1)	(110,000)	—

NOTES TO FINANCIAL STATEMENTS

Note 1—Marketable Equity Securities

At December 31, 1975, the current and noncurrent portfolios of marketable equity securities are each carried at their lower of cost or market at the balance sheet date. Marketable equity securities included in current and noncurrent assets had a cost of $900,000 and $650,000, respectively, at December 31, 1975.

To reduce the carrying amount of the current marketable equity securities portfolio to market, which was lower than cost at December 31, 1975, a valuation allowance in the amount of $50,000 was established with a corresponding charge to net income at that date. To reduce the carrying amount of the noncurrent marketable equity securities portfolio to market, which was lower than cost at December 31, 1975, a valuation allowance in the amount of $110,000 was established by a charge to stockholders' equity representing the net unrealized loss.

At December 31, 1974, the current and noncurrent portfolios of marketable equity securities were not required to be carried at their lower of cost or market at the balance sheet date and were carried at cost. Marketable equity securities included in current and noncurrent assets had a market value of $925,000 and $500,000, respectively, at December 31, 1974.

At December 31, 1975, gross unrealized gains and gross unrealized losses pertaining to the marketable equity securities in the portfolios were as follows:

	Gains	Losses
Current	$75,000	$125,000
Noncurrent	$90,000	$200,000

A net realized loss of $10,000 on the sale of marketable equity securities was included in the determination of net income for 1975. The cost of the securities sold was based on the average cost of all the shares of each such security held at the time of sale. There were no sales of marketable equity securities during 1974.

APPENDIX B

INTERPRETATIONS OF FASB STATEMENT NO. 12

FASB INTERPRETATION NO. 10
APPLICATION OF FASB STATEMENT NO. 12
TO PERSONAL FINANCIAL STATEMENTS

September 1976

Introduction

1. Paragraph 5 of *FASB Statement No. 12*, "Accounting for Certain Marketable Securities," enumerates the entities excluded from the scope of the Statement but does not mention individuals. The AICPA Industry Audit Guide, "Audits of Personal Financial Statements," states that ". . . financial statements for individuals should be prepared on a cost basis, in conformity with generally accepted accounting principles" and that ". . . financial information on an estimated value basis is useful . . . as additional financial information" (pages 2 and 3). Further, the Industry Audit Guide recommends a two-column presentation of personal financial statements: "The first column should present financial data on the cost basis, paralleled by a second column presenting estimated values" (page 3). The FASB has been asked to clarify whether in personal financial statements prepared in conformity with generally accepted accounting principles the presentation of marketable equity securities on an estimated value basis in the second column supplants the requirement of paragraph 8 of *FASB Statement No. 12* to carry marketable equity securities at the lower of aggregate cost or aggregate market value in the first column.

Interpretation

2. Personal financial statements prepared in conformity with generally accepted accounting principles are included in the scope of *FASB Statement No. 12*. The presentation of marketable equity securities on an estimated value basis as additional financial information in the second column does not supplant the requirement of paragraph 8 of *FASB Statement No. 12* to carry marketable equity securities at the lower of aggregate cost or aggregate market value in the first column.

Effective Date and Transition

3. The provisions of this Interpretation shall be effective for financial statements for annual and interim periods ending after October 15, 1976. Earlier application is encouraged in financial statements for annual and interim periods ending before October 16, 1976 that have not been previously issued. This Interpretation shall not be applied retroactively for previously issued annual or interim financial statements.

This Interpretation was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.

Marshall S. Armstrong, *Chairman*
Oscar S. Gellein
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
Robert T. Sprouse

FASB INTERPRETATION NO. 11
CHANGE IN MARKET VALUE AFTER THE BALANCE SHEET DATE

September 1976

Introduction

1. Paragraphs 13 and 17[1] of *FASB Statement No. 12*, "Accounting for Certain Marketable Securities," specify in part that "an enterprise's financial statements shall not be adjusted for realized gains or losses or for changes in market prices with respect to marketable equity securities when such gains or losses or changes occur after the date of the financial statements but prior to their issuance, except for situations covered by paragraph 21." The Board has been requested to clarify the meaning of the qualification, *except for situations covered by paragraph 21*.

2. Paragraph 21 of *FASB Statement No. 12* states:

> For those marketable securities for which the effect of a change in carrying amount is included in stockholders' equity rather than in net income (including marketable securities in unclassified balance sheets), a determination must be made as to whether a decline in market value below cost as of the balance sheet date of an individual security is other than temporary. . . . If the decline is judged to be other than temporary, the cost basis of the individual security shall be written down to a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in market value.

The Board also has been asked to elaborate on the amount of the write-down that shall be accounted for as a realized loss when the "decline in market value below cost *as of the balance sheet date* of an individual security is other than temporary." (Emphasis added.)

Interpretation

3. In the case of those marketable securities for which the effect of a change in carrying amount is included in stockholders' equity rather than in net income, the phrase "except for situations covered by paragraph 21" in paragraphs 13 and 17 refers to the provisions in paragraph 21 requiring a decline in market value below cost as of the balance sheet date of an individual security that is determined to be other than temporary to be accounted for as a realized loss. In judging whether a decline in market value below cost at the balance sheet date is other than

[1]Paragraph 13 applies to enterprises in industries not having specialized accounting practices with respect to marketable securities, and paragraph 17 applies to enterprises in industries having specialized accounting practices with respect to marketable securities.

temporary, a gain or loss realized on subsequent disposition or changes in market price occurring after the date of the financial statements but prior to their issuance shall be taken into consideration along with other factors.

4. The amount of decline in market value below cost of an individual marketable equity security that is accounted for as a realized loss as of the balance sheet date because the decline is other than temporary shall not exceed the difference between market value at the balance sheet date and cost of the marketable equity security. Further declines in market value after the balance sheet date might indicate that the decline in market value below cost at the balance sheet date was other than temporary. However, those declines result from information, events, or changes in expectations occurring after the balance sheet date. Accordingly, if a decline in market value below cost as of the balance sheet date of an individual security is judged to be other than temporary, further declines in market value occurring after the date of the balance sheet shall not be included in the amount that is accounted for as a realized loss as of the balance sheet date. Recoveries in market value after the balance sheet date also result from information, events, or changes in expectations occurring after the balance sheet date, but they tend to indicate that a portion or all of the decline at the balance sheet date was in fact temporary. Accordingly, such recoveries shall be considered when estimating the amount of decline as of the balance sheet date that is judged to be other than temporary.

Effective Date and Transition

5. The provisions of this Interpretation shall be effective for financial statements for annual and interim periods ending after October 15, 1976. Earlier application is encouraged in financial statements for annual and interim periods ending before October 16, 1976 that have not been previously issued. This Interpretation shall not be applied retroactively for previously issued annual or interim financial statements.

This Interpretation was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.

Marshall S. Armstrong, *Chairman*
Oscar S. Gellein
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
Robert T. Sprouse

FASB INTERPRETATION NO. 12
ACCOUNTING FOR PREVIOUSLY ESTABLISHED ALLOWANCE ACCOUNTS

September 1976

Introduction

1. Paragraph 8 of *FASB Statement No. 12*, "Accounting for Certain Marketable Securities," specifies that the "carrying amount of a marketable equity securities portfolio shall be the lower of its aggregate cost or market value, determined at the balance sheet date." Paragraph 7(e) of *FASB Statement No. 12* defines "cost" of a marketable equity security as "original cost . . . unless a new cost basis has been assigned based on recognition of an impairment of value that was deemed other than temporary. . . . In such cases, the new cost basis shall be the cost. . . ."

2. Prior to the issuance of *FASB Statement No. 12*, some enterprises that carried marketable equity securities at cost had reduced the carrying amount of individual marketable equity securities to market value through an allowance account with a corresponding amount included in the determination of net income. In some of those cases, a new cost basis was not established for individual securities and the allowance account was expected to increase or decrease depending on fluctuations in the market price of the marketable equity security because the decline in market value below cost was assessed to be temporary. The Board has been asked to clarify whether, in those cases, the original cost of the individual securities or the original cost reduced by an existing allowance account should be used in applying paragraphs 7(e) and 8 of *FASB Statement No. 12*.

Interpretation

3. The original cost of individual marketable equity securities shall be used in applying paragraphs 7(e) and 8 of *FASB Statement No. 12* by an enterprise that carried marketable equity securities at cost and that (a) had reduced the carrying amount of individual marketable equity securities through an allowance account with a corresponding amount included in the determination of net income prior to the effective date of the Statement and (b) expected the allowance account to increase or decrease in the future based on fluctuations in the market price of the security because the decline in market value below cost was assessed to be temporary. Any balance remaining in such an existing allowance account shall be eliminated and credited to income in the period in which this Interpretation is initially applied. The valuation allowance would then be determined in accordance with paragraph 8 of *FASB Statement No. 12*.

4. If, prior to the effective date of *FASB Statement No. 12*, a new cost basis had been assigned to a marketable equity security based on recognition of an impairment of value that was deemed other than temporary, the new cost basis shall be used in applying the provisions of *FASB Statement No. 12*.

Effective Date and Transition

5. The provisions of this Interpretation shall be effective for financial statements for annual and interim periods ending after October 15, 1976. Earlier application is encouraged in financial statements for annual and interim periods ending before October 16, 1976 that have not been previously issued. This Interpretation shall not be applied retroactively for previously issued annual or interim financial statements.

The Interpretation was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.

Marshall S. Armstrong, *Chairman*
Oscar S. Gellein
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
Robert T. Sprouse

FASB INTERPRETATION NO. 13
CONSOLIDATION OF A PARENT AND ITS SUBSIDIARIES HAVING DIFFERENT BALANCE SHEET DATES

September 1976

Introduction

1. Paragraphs 8, 9, and 15 of *FASB Statement No. 12,* "Accounting for Certain Marketable Securities," set forth the requirements of the portfolio basis for comparing cost and market value. The portfolio basis requires that marketable equity securities owned by enterprises that are consolidated and that do not follow specialized accounting practices with respect to marketable equity securities, or that are consolidated and follow the same specialized accounting practices with respect to marketable equity securities, shall be aggregated into separate portfolios according to the current or noncurrent classifications of the securities. The aggregate cost and aggregate market value of the portfolios are compared to determine carrying amount.

2. Paragraph 13 of *FASB Statement No. 12,* which applies to enterprises in industries not having specialized accounting practices with respect to marketable securities, states:

> An enterprise's financial statements shall not be adjusted for realized gains or losses or for changes in market prices with respect to marketable equity securities when such gains or losses or changes occur after *the date of the financial statements* but prior to their issuance, except for situations covered by paragraph 21. However, significant net realized and net unrealized gains and losses arising after *the date of the financial statements,* but prior to their issuance, applicable to marketable equity securities owned at the date of the most recent balance sheet shall be disclosed. (Emphasis added.)

Paragraph 17 of *FASB Statement No. 12,* which applies to enterprises in industries having specialized accounting practices with respect to marketable securities, is in substance identical to paragraph 13 of the Statement.

3. The financial statements of a subsidiary sometimes are consolidated with the financial statements of its parent even though the financial statements of the subsidiary are as of a date different from the financial statements of the parent. The use of different dates is permitted by paragraph 4 of *ARB No. 51,* "Consolidated Financial Statements," which states:

> A difference in fiscal periods of a parent and a subsidiary does not of itself justify the exclusion of the subsidiary from consolidation. It ordinarily is feasible for the subsidiary to prepare, for consolidation purposes, statements for a period which corresponds with or closely approaches the fiscal period of the parent. However, where the difference is not more than about three months, it usually is acceptable to use, for consolidation purposes, the subsidiary's statements for its fiscal period; when this is done, recognition should be given by disclosure or otherwise to the effect of intervening events which materially affect the financial position or results of operations.

4. The Board has been requested to clarify application of the portfolio basis specified in *FASB Statement No. 12* when the financial statements of a subsidiary are as of a date different from that of its parent and are consolidated with the financial statements of its parent. Further, the Board has been asked to explain the meaning of "the date of the financial statements" in paragraphs 13 and 17 of *FASB Statement No. 12* when the financial statements of a subsidiary or investee are as of a date different from that of its parent or investor and are consolidated with or accounted for by the equity method in the financial statements of its parent or investor.

Interpretation

5. To compute the amount of any valuation allowance(s) required by *FASB Statement No. 12* in the consolidated financial statements, aggregate cost and aggregate market value of the portfolio(s) shall be determined for each subsidiary that is consolidated as of the date of each subsidiary's balance sheet, and those aggregates shall be combined with aggregate cost and aggregate market value of the parent's portfolio(s) determined as of the parent's balance sheet date. For example, assume that consolidated financial statements dated December 31, 1976 and issued on March 1, 1977 include the financial statements of the parent as of December 31, 1976 and of the subsidiary as of October 31, 1976. The cost of the marketable equity securities owned by the subsidiary at October 31, 1976 is added to the cost of the marketable equity securities owned by the parent at December 31, 1976. The market values at October 31, 1976 of the securities owned by the subsidiary and the market values at December 31, 1976 of the securities owned by the parent are aggregated in the same manner. The aggregate cost and aggregate market value of the portfolios are compared to determine the carrying amount in the consolidated financial statements.

6. For purposes of applying paragraphs 13 and 17 of *FASB Statement No. 12*, "the date of the financial statements" shall be for each subsidiary or investee the date of the financial statements that are consolidated with or accounted for by the equity method in the financial statements of its parent or investor. The last sentence in each of those paragraphs requires disclosure of significant net realized gains or losses and of significant net unrealized gains or losses arising after the date of the financial statements. Using the assumptions in the example in paragraph 5 above, aggregate amounts are computed as follows for possible disclosure: the net *realized* gains or losses arising after October 31, 1976 and prior to March 1, 1977 applicable to the marketable equity securities in the portfolio of the subsidiary at October 31, 1976 are aggregated with the net *realized* gains or losses arising after December 31, 1976 and prior to March 1, 1977 applicable to the marketable equity securities in the portfolio of the parent at December 31, 1976. Likewise, net *unrealized* gains or losses arising in the portfolio of the subsidiary after October 31, 1976 and prior to March 1, 1977 applicable to the marketable equity securities in the portfolio of the subsidiary at October 31, 1976 are aggregated with the net *unrealized* gains or losses arising after December 31, 1976 and prior to March 1, 1977 applicable to the marketable equity securities in the portfolio of the parent at December 31, 1976. If significant, each of the aggregate amounts shall be disclosed.

7. If the financial statements of a subsidiary are consolidated with the financial statements of its parent and the financial statements of the subsidiary are as of a date different from the financial statements of the parent, paragraph 4 of *ARB No. 51* requires that "recognition should be given by disclosure or otherwise to the effect of intervening events which materially affect the financial position or results of operations." In the case of the subsidiary in the example in paragraph 5 above, that requirement pertains to the period from October 31, 1976 to December 31, 1976. Accordingly, in addition to the disclosure required by paragraph 6 above, the net realized gains or losses and the net unrealized gains or losses arising after October 31, 1976 and prior to December 31, 1976 applicable to the marketable equity securities of the subsidiary shall be disclosed if they "materially affect the financial position or results of operations." Further, as required by paragraphs 13 and 17 of *FASB Statement No. 12*,[1] the subsidiary's financial statements shall not be adjusted for realized gains or losses or for changes in market prices with respect to its marketable equity securities occurring after October 31, 1976 and prior to December 31, 1976, unless the decline in market value below cost of an individual marketable equity security is determined to be other than temporary and, accordingly, shall be accounted for as a realized loss.

[1]See also *FASB Interpretation No. 11*, "Changes in Market Value after the Balance Sheet Date: an interpretation of FASB Statement No. 12."

Effective Date and Transition

8. The provisions of this Interpretation shall be effective for financial statements for annual and interim periods ending after October 15, 1976. Earlier application is encouraged in financial statements for annual and interim periods ending before October 16, 1976 that have not been previously issued. This Interpretation shall not be applied retroactively for previously issued annual or interim financial statements.

This Interpretation was adopted by the unanimous vote of the six members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.

Marshall S. Armstrong, *Chairman*
Oscar S. Gellein
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
Robert T. Sprouse

APPENDIX C

AUDITING INTERPRETATIONS

The Institute staff has been authorized to issue interpretations of auditing questions having general interest to the profession. The purpose of the interpretations is to provide guidance on a timely basis without the formal procedures required for a Statement on Auditing Standards and to clarify points on which past practice may have varied and been considered generally accepted. These interpretations, which are reviewed with informed members of the profession, are not pronouncements of the Auditing Standards Executive Committee. However, members should be aware that they may be called upon to justify departures from the interpretations. Interpretations are prepared by the auditing standards division and the technical research division. Unless otherwise stated, the interpretations are not intended to be retroactive.

EVIDENTIAL MATTER FOR LONG-TERM INVESTMENTS: AUDITING INTERPRETATIONS OF AU SECTION 332

1. Evidential Matter for the Carrying Amount of Marketable Securities

.01 *Question*—Section 332.03, states: "With respect to the carrying amount of [long-term] investments, a loss in value which is other than a temporary decline should be recognized in the financial statements of an investor." AC section 2031.09 [Volume 3, AICPA PROFESSIONAL STANDARDS], with respect to working capital and current assets, states: "In the case of marketable securities where market value is less than cost by a substantial amount and it is evident that the decline in market value is not due to a mere temporary condition, the amount to be included as a current asset should not exceed the market value." What evidence should the auditor obtain pertaining to the classification and the carrying amount of marketable securities when market value is below cost?

.02 *Interpretation*—Section 509.21 states: "In preparing financial statements, management is expected to use its estimates of the outcome of future events." Estimates of the outcome of future events include determining the proper carrying amount for securities when market value is below cost. The auditor should examine evidence to determine whether management properly classified the marketable securities as current or noncurrent assets and whether the amounts at which they are carried in the financial statements are appropriate. The auditor should evaluate the reasons for the market decline when market value is below cost.

.03 Declines in market value may be temporary in nature or may reflect conditions that are more persistent. The distinction between temporary and persistent, however, has been largely undefined. Declines may result primarily from daily market fluctuations or from short-term variations in general economic or market conditions that are temporary in nature. Declines may also be attributable to general economic and money market conditions that persist for other than a temporary time period. Other market declines may be attributable to specific adverse conditions that affect a particular company's securities.

.04 *Classification of Securities*—The classification of marketable securities as either current assets or noncurrent assets is an important consideration in evaluating their proper carrying amounts. Whether marketable securities are properly classified depends to a large extent on management's intent. If management intends to dispose of the securities in the next fiscal year, the securities are classified as a current asset. Marketable securities that represent an excess of funds available for operations, but which management does not intend to dispose of, are often classified as current assets since management can sell them at any time at their option.

.05 The auditor should ascertain management's investment objectives to determine whether the securities are properly classified in the financial statements. He should read the minutes of the board of directors meetings, and he should inquire of the investment committee concerning management's intentions on disposing of the securities. To corroborate management's representation as to its intent, the auditor should consider whether such classification is feasible in light of the company's financial position, working capital requirements, debt agreements, and any other contractual obligations. The client's needs may be such that it is reasonable to presume that the securities will need to be sold to raise operating capital, and consequently should be classified as current assets.

.06 The auditor should obtain management's representation as to their intent in the client's representation letter. In some circumstances, the classification in the balance sheet should be supplemented by additional information in the notes to the financial statements regarding management's intent to make the financial statements more meaningful to users. The auditor should evaluate the adequacy of disclosures concerning classification of investments in securities and consider the need for such disclosures.

.07 *Investments Classified as Current Assets.* Marketable securities, such as stocks and bonds, properly classified as current assets should be written down to market at the balance sheet date to reflect declines that are not temporary in accordance with AC section 2031.09 [Volume 3, AICPA PROFESSIONAL STANDARDS]. When marketable securities classified as a current asset have a market value lower than cost, retention of the cost basis requires persuasive evidence that indicates a recovery in the market value will occur before the earlier of the scheduled maturity or sale date of the securities or within a one-year period from the balance sheet date. Generally, such evidence would be limited to substantial recovery subsequent to the year end. When such evidence does not exist and the client's management carries those securities at cost, the auditor will normally conclude that he does not agree with management's determination of the carrying amount of the securities. Section 509.21 states: "If the auditor, on the basis of evidence available to him, disagrees with management's determination, and if the effects on the financial statements are material, he should express a qualified or an adverse opinion because of a departure from generally accepted accounting principles."

.08 *Investments Classified as Noncurrent Assets.* Investments in marketable securities that are properly classified as noncurrent assets should be carried at amounts that result in a fair presentation in conformity with generally accepted accounting principles. If there has been a decline in the market value of those investments, the auditor should obtain evidence concerning the nature of the decline. In making that determination, he should consider the ability to ultimately recover the carrying amount of the investments.

.09 When the market decline is attributable to specific adverse conditions for a particular security, stocks or bonds, a write down in carrying amount is necessary unless persuasive evidence exists to support the carrying amount.

.10 The value of investments in marketable securities classified as noncurrent assets may decline because of general market conditions that reflect prospects of the economy as a whole or prospects of a particular industry. Such declines may or may not be indicative of the ability to ultimately recover the carrying amount of investments. The auditor should consider all available evidence to evaluate the carrying amount of the securities. For investments in bonds and other investments with fixed maturity amounts, market declines may be considered temporary unless the evidence indicates that such investments will be disposed of before they mature or that they may not be realizable.

.11 If the auditor concludes the available information does not support either a judgment as to eventual recovery or a contrary judgment that recovery will not occur, the continued existence of a decline in market value is indicative of an uncertainty, as described in section 509.22. "In certain instances, the outcome of matters that may affect the financial statements or the disclosures required therein is not susceptible of reasonable estimation; such matters are to be regarded as uncertainties. . . . When such uncertainties exist, it cannot be determined whether the financial statements should be adjusted, or in what amount." The auditor should appropriately qualify his opinion because of the uncertainty of recovering the carrying amount of the asset. A qualification based on the uncertainty of recoverability, however, is not a substitute for recognition of a loss when such recognition is appropriate.

.12 *Reclassifications of Investments.* Management may classify as a noncurrent asset a security that was classified in the previous year's financial statements as a current asset. Such a change in classification does not require the auditor to qualify his opinion as to consistency if it results from additional experience and information acquired in the current year (see section 420.12). For example, management may conclude that the decline in market value will eventually be recovered and decide not to dispose of the security until its market value recovers. If the change in classification is material, the auditor should evaluate the adequacy of disclosure explaining the change (see section 420.14).

.13 *Unclassified Balance Sheets.* Companies in some industries, such as insurance, investment, finance, and real estate do not present classified balance sheets. The representations made by management in an unclassified balance sheet differ from those made in a classified balance sheet. For example, inclusion of an asset in the current assets section of a classified balance sheet implies that those assets will be, or can be, converted into cash in a specified period. Therefore, if the amount to be realized from converting those assets appears to be impaired, generally accepted accounting principles require that they should be written down to their market values. In an unclassified balance sheet, no representations are made about working capital as of the balance sheet date.

.14 If securities are carried at cost in an unclassified balance sheet, the auditor should consider the operational needs of the company for the foreseeable future. For those securities that will be disposed of in the foreseeable future the auditing considerations are similar to those for marketable securities classified as current assets. For those securities for which there is no evidence indicating that they will be disposed of in the foreseeable future to meet the company's operational needs, the auditing considerations are similar to those discussed for marketable securities classified as noncurrent assets.

[Issue date: January, 1975.]

INDEX